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No. 05-051221

IN THE

Supreme Court of the United States

PRESTON MARTIN, ROY DOUMANI, BEVERLY W. THRALL (Successor to the Claims of Larry B. Thrall), ARBUR, INC., WILLIAM E. SIMON, JR., J. PETER SIMON, AND GEORGE J. GILLESPIE, III (Executors of the Estate of William E. Simon, Sr.),

Petitioners,

v.

UNITED STATES, *et al.*,

Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether recovery for losses caused by breach of a Government contract, even when the losses are foreseeable as a factual matter, is barred as a legal matter unless the contract itself specifically obliged the harmed party to incur those losses upon breach or the loss is of property the contract obliged the harmed party to acquire.

2. Whether Government resolutions that approve a financial transaction with the Government, address particular persons who made the offer to the Government, and impose obligations on such persons as a condition of approval create a contract enforceable by those persons.

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

Besides the named petitioners and respondent, two corporations were parties to the proceedings below: Southern California Federal Savings Loan Association ("SoCal") and SoCal Holdings, Inc. ("SCH"), which in 1997 changed their names to People's Bank of California and PBOC Holdings, Inc., respectively. In 2001, the People's Bank of California merged into California National Bank, which became the successor in interest to SoCal. The foregoing institutions, whose rights are not at issue in this petition, have settled their claims in this case.

Of the named petitioners, only one is a corporation, namely, Arbur, Inc. It is a closely held Simon-family corporation with no parent corporations and no publicly held company holding 10% or more of its stock. *See* S. Ct. Rule 29.6.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT	ii
TABLE OF AUTHORITIES	v
OPINIONS BELOW	1
JURISDICTION	1
STATEMENT	1
A. Background	2
B. Trial Court Proceedings	9
C. The Court of Appeals Decision	12
REASONS FOR GRANTING THE PETITION	15
I. THE FEDERAL CIRCUIT'S RESTRICTION OF CONTRACT REMEDIES TO DENY RECOVERY FOR FORESEEABLE LOSS CAUSED BY BREACH SHOULD BE REVIEWED	18
A. The Decision Is Inconsistent With The Governing Law Of Contract Remedies	18
B. The Decision Creates Lower Court Doctrinal Conflicts	22
C. It Is Important To Correct This Decision By The Appellate Court With Special Authority Over Government Contracts	25
II. THE FEDERAL CIRCUIT'S REJECTION OF CONTRACT RIGHTS BASED ON THE BANK BOARD'S APPROVAL RESOLUTIONS SHOULD BE REVIEWED	26

TABLE OF CONTENTS—Continued

	Page
CONCLUSION	30
APPENDICES	
APPENDIX A: Federal Circuit Opinion	1a
APPENDIX B: Court of Federal Claims Damages Opinion	31a
APPENDIX C: Court of Federal Claims Liability Opinion	125a
APPENDIX D: Federal Circuit Rehearing Denial	176a
APPENDIX E: Regulatory Capital Maintenance Agreement	178a
APPENDIX F: FHLBB Resolutions and Forbearance Letter	197a

TABLE OF AUTHORITIES

CASES Pages

Bluebonnet Savings Bank, F.S.B. v. United States, 266 F.3d 1348 (Fed. Cir. 2001)..... 10, 22-23
Cain v. United States, 350 F.3d 1309 (Fed. Cir. 2003)..... 29
California Fed. Bank, FSB v. United States, 245 F.3d 1342 (Fed. Cir. 2001)..... 29
Data Enters. of the Northwest v. GSA, 2004 WL 323922 (GSBCA No. 15607)..... 24
Fidelity & Deposit Co. v. Krebs Engineers, 859 F.2d 501 (7th Cir. 1988)..... 20
Home Savings of America v. United States, 399 F.3d 1341 (Fed. Cir. 2005)..... 24, 28-29
Indiana Michigan Power Co. v. United States, 422 F.3d 1369 (Fed. Cir. 2005)..... 24
Landmark Land Co. v. FDIC, 256 F.3d 1365 (Fed. Cir. 2001)..... 24
La Van v. United States, 382 F.3d 1340 (Fed. Cir. 2004)..... 10, 23-24, 29
Lynch v. United States, 292 U.S. 571 (1934)..... 18
Massie v. United States, 166 F.3d 1184 (Fed. Cir. 1999)..... 29
Mobil Oil Exploration & Producing Southeast, Inc. v. United States, 530 U.S. 604 (2000)..... *passim*
Northern Helex Co. v. United States, 524 F.2d 707 (Ct. Cl. 1975)..... 24
Perry v. United States, 294 U.S. 330 (1935)..... 18
Prudential Ins. Co. of America v. United States, 801 F.2d 1295 (Fed. Cir. 1986)..... 24
Strougo v. Bassini, 282 F.3d 162 (2d Cir. 2002)... 10
Trauma Serv. Group v. United States, 104 F.3d 1321 (Fed. Cir. 1997)..... 29
United States v. Winstar Corp., 518 U.S. 839 (1996)..... *passim*

TABLE OF AUTHORITIES

STATUTES	Pages
28 U.S.C. § 1254(1)	1
§ 1295(a)(2)	25
§ 1295(a)(3)	25
§ 1295(a)(10)	25
§ 1346(a)(2)	25
§ 1491(a)	25

OTHER AUTHORITIES

Restatement (Second) of Contracts (1979)

§§ 17-24	28
§ 50	28
§§ 71-72	28
§ 202	18
§ 243	9, 18
§ 250	18
§§ 256-257	18
§ 261	18
§ 264	18
§ 344	19, 20, 23
§ 346	18, 19
§ 347	13, 19, 23
§ 349	20
§§ 350-353	19
§ 351	19, 23, 24
§ 352	23
§ 373	18
§§ 357-359	18

PETITION FOR A WRIT OF CERTIORARI

The parties referred to below as the "Individual Plaintiffs" petition this Court for a writ of certiorari to review the judgment of the United States Court of Appeals for the Federal Circuit in this case.

OPINIONS BELOW

The Federal Circuit's opinion (App. 1a-30a) is reported at 422 F.3d 1319. The damages opinion of the Court of Federal Claims (App. 31a-124a) is reported at 57 Fed. Cl. 598. The liability opinion of the Court of Federal Claims (App. 125a-75a) is reported at 52 Fed. Cl. 531.

JURISDICTION

The corrected judgment of the court of appeals was entered on August 30, 2005. App. 1a. A timely petition for panel and en banc rehearing was denied on December 27, 2005. App. 176a-77a. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATEMENT

This case is one of roughly 120 cases that have arisen out of conduct addressed in *United States v. Winstar Corp.*, 518 U.S. 839 (1996), which affirmed breach-of-contract judgments against the United States. Petitioners were investors who successfully rescued a savings and loan (thrift) in 1987, saving the Government, as insurer, from the consequences of the thrift's collapse. They did so under a Government contract that guaranteed permission to count certain capital toward satisfying regulatory requirements. When the Government breached the contract by withdrawing that permission, the thrift had to raise new capital, and part of the price for that capital was the obliteration of petitioners' 1987 equity stake, so that the contributors of the new capital would benefit if the thrift's fortunes turned around, which they did.

This petition seeks review of the Federal Circuit's holding that, although the Government had a contract with petitioners and breached it, petitioners could not recover for the loss of their 1987 equity stake as a matter of law. The Federal Circuit denied petitioners their due by adopting an unprecedented and unjustified narrowing of the fundamental contract-damages principle that an injured party should be placed in the position it would have occupied had the contract been performed rather than breached. The court also strayed from familiar contract law on formation of contracts, ignoring the full scope of petitioners' contract rights. This Court should review the decision in this case, as it reviewed the Federal Circuit's comparable departure from ordinary commercial contract law in *Mobil Oil Exploration & Producing Southeast, Inc. v. United States*, 530 U.S. 604 (2000), in order to enforce and re-establish the bedrock rights of parties to Government contracts, as recognized in this very context by *Winstar*.

A. Background

1. In 1985, an insolvent thrift in California, insured by the Federal Savings and Loan Insurance Corporation (FSLIC), was placed in FSLIC's receivership by FSLIC's governing board, the Federal Home Loan Bank Board (FHLBB, or Bank Board). To avoid liquidating the thrift and incurring the high insurance costs, the FHLBB spent well over a year seeking buyers of the thrift. In late 1986, petitioners (or their predecessors)—a group called the "Individual Plaintiffs" below, which included Preston Martin, former Federal Reserve Vice-Chairman and former FHLBB Chairman, and William E. Simon, Sr., former Secretary of the Treasury—responded with a bid, which the FHLBB approved. App. 4a-5a, 33a-34a, 126a-27a.[1] The deal was one of many "'supervisory

[1] One of the petitioners, Arbur, Inc., is a Simon-family-owned corporation treated as one of the "Individual Plaintiffs." Arbur and Secretary

mergers'" in which "the Bank Board chose to avoid the insurance liability by encouraging healthy thrifts and outside investors to take over ailing institutions." *Winstar*, 518 U.S. at 847 (principal opinion).

The transaction in this case, with its multiple related parts, was consummated in April 1987. On the same day, the FHLBB approved the conversion of the old (mutual) thrift into a common-stock thrift, Southern California Federal Savings and Loan Association (SoCal), and the acquisition of all its stock by a holding company, SoCal Holdings, Inc. (SCH), which petitioners had just formed for the sole purpose of buying SoCal. App. 5a, 127a, 197a, 202a-04a (FHLBB Res. 87-511).[2] As expressed in the FHLBB resolutions and "key" agreement, App. 41a, 133a, petitioners themselves, not only SoCal and SCH, had a bargain with the Government in taking on this role of saving the thrift from liquidation at the Government's expense.

The Government's principal commitment, as far as this case (like other *Winstar* cases) is concerned, was the promise that the thrift could account in a certain way for "regulatory

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Simon's estate are the "Simon Plaintiffs," and Roy Doumani, Preston Martin, and Beverly W. Thrall (successor to her late husband, original investor Larry B. Thrall) are the "DMT Plaintiffs." Together, the two groups constitute the Individual Plaintiffs—as distinguished from the thrift and its holding company, the "Institutional Plaintiffs." *See* App. 2a, 127a. For simplicity, this petition hereafter refers to "petitioners" to include their predecessors (Secretary Simon, in the case of his estate; Larry B. Thrall, in the case of Beverly W. Thrall).

[2] The FHLBB initially called the new thrift "New Association," using "SoCal" for the old thrift. Because the thrift's name remained essentially unchanged, however, throughout this litigation "SoCal" has been used to name the new thrift, and this petition follows suit.

SCH was formed two months earlier—*after* the FHLBB had accepted petitioners' bid in principle—for the sole purpose of acquiring SoCal, as stated in its application to the FHLBB (JX 1381 p. 2) and the main FHLBB approval resolution (App. 197a). App. 130a.

capital," the amount of capital that the thrift is legally required to have in its possession. App. 5a. In this case, the Government's approval resolutions themselves promised to allow the counting of almost $300 million in "capital credits" ($217.5 million) and "supervisory goodwill" ($79 million) as regulatory capital, without which the thrift would have been severely undercapitalized. App. 132a, 133a, 210a, 217a; App. 224a-26a ("Forbearance Letter" to petitioner Martin, chairman and CEO of SCH); *see Winstar*, 518 U.S. at 847-56 (principal opinion). In return, the Government, relying on the personal credentials of petitioners, secured various personal promises from petitioners as part of the bargain, again reflected in the approval resolutions. App. 5a; App. 42a ("The experience and reputation of Secretary Simon's investment group was considered an important intangible asset in the rejuvenation of the thrift.").

The contract between the Government and petitioners had two components that are at issue here. One is a Regulatory Capital Maintenance Agreement (RCMA), App. 178a-96a, which the Government entered into with petitioners, as well as with SoCal and SCH, as signatory parties. App. 5a, 132a; *see* App. 19a ("the Individual Plaintiffs . . . were in contractual privity with the government under the RCMA"). The other is the FHLBB approval resolutions themselves. The RCMA, the FHLBB approval, and SCH's purchase of SoCal all occurred on April 30, 1987. App. 180a ("Stock Purchase Agreement of even date herewith"). The overall transaction thus had several simultaneous, interdependent parts.[3]

[3] The Government also entered into an Assistance Agreement that was signed only by SoCal, SCH, and FSLIC, under which the FHLBB furnished certain financial assistance to the new thrift. *See* App. 5a. This petition does not rely on that agreement.

The RCMA shows the Government's reliance on petitioners personally and the key regulatory-capital guarantee:

- "First, Recital A indicates that 'the [Individual Plaintiffs] collectively own 97.5 percent of the outstanding voting securities of [SCH] and control [SCH].'" App. 19a, quoting App. 180a.
- "Second, Recital G and § 1 include the government's promise that SCH and SoCal will be able to account for $217.5 million in capital credits as part of its regulatory capital." App. 19a. (The separate goodwill guarantee, set out in the main FHLBB approval resolution, was not mentioned in the RCMA.) Section 1 also requires the thrift and its holding company to meet prescribed regulatory-capital levels. *See* App. 5a, 181a-83a.
- "Third, the RCMA states that 'so long as [SCH] shall be obligated pursuant to § 1, the [Individual Plaintiffs], severally in proportion to their initial ownership of the common stock of [SCH] . . ., hereby guarantee the performance of [SCH] and [SoCal] under § 1,'" up to an aggregate limit of $5 million. App. 19a; *see* App. 5a-6a, 41a, 132a, 183a-84a.
- Fourth, "the RCMA requires that the Individual Plaintiffs, or their successors who have assumed their shares of the guarantee and have not been objected to by the FSLIC, shall 'collectively own not less than a majority of the outstanding voting power of [SCH].'" App. 19a-20a; *see* App. 184a-85a. The RCMA also details the remedy for violation of that promise: petitioners forfeit their stock to the Government, which repossesses the thrift and its holding company. *See* App. 186a-89a.
- Finally, the RCMA specifies that the just-described provision for forfeiture and repossession applies also if SoCal's regulatory capital falls below 3% of its Total Liabilities. App. 187a-89a; *see* App. 42a, 132a;

App. 41a, 133a (provision is "key to understanding the deal").

Like the RCMA, the key FHLBB approval resolution, which finds that the SoCal thrift was a failing institution and approves the transaction as "lessen[ing] the risk to the FSLIC" (App. 215a) and "necessary to prevent the probable failure" of the thrift (App. 217a), directly addresses not only SCH and SoCal but also petitioners, whose "offer" it accepts (App. 215a). It grants the special permission some petitioners needed to play their roles in SoCal (App. 198a-200a, 212a-14a); requires petitioners to execute the RCMA, which it notes provides petitioners' guarantee and contains a stock-forfeiture remedy (App. 201a, 204a); requires petitioners to supply an opinion of counsel that the Assistance Agreement and RCMA have been executed and "constitute valid and binding obligations of SoCal Holdings and the Investors [petitioners]" (App. 206a); and demands certain additional certifications from petitioners (App. 206a-07a). *See* App. 203a, 211a (FHLBB "has considered the financial and managerial resources" of SoCal and SCH), 220a (Res. No. 87-513 addressing petitioners), 40a, 132a. Among the FHLBB commitments in the key approval resolution is the favorable regulatory-capital treatment of *both* capital credits *and* intangible assets (goodwill). App. 210a, 217a.

2. After the 1987 transaction, the new SoCal, owned and controlled by petitioners, made great strides toward regaining financial health. App. 6a ("By 1989, SoCal's financial situation had improved greatly."); App. 43a-48a. But in 1989, the Government, by statute and implementing regulations, changed the permitted treatment of regulatory capital on which investments like petitioners' were based. *Winstar*, 518 U.S. at 856-58 (principal opinion). The changes required the quick phasing out of recognition of the capital credits and supervisory goodwill that were key to petitioners' involvement in 1987. App. 4a, 48a-49a, 51a, 134a-35a.

In this case, SoCal was in compliance with regulatory capital requirements before the 1989 changes took place. App. 50a-52a. Indeed, SoCal had an excess of $188 million in regulatory capital. App. 50a-51a. The 1989 legal changes, however, made SoCal's capital severely inadequate and rendered it a troubled institution. App. 6a, 50a.

With the legal changes substantially impairing SoCal's operations, App. 53a-56a, the institution had to address, and did address, its regulatory-capital shortfall in two ways. One was to shrink, thereby lowering the amount of capital that was legally required. But SoCal could not shrink fast enough, and so SoCal and SCH had no choice but to pursue the second response: to raise new capital, without which the existing equity would have been worthless. App. 6a, 56a-62a. That response, forced by the breach, destroyed petitioners' 1987 equity in two steps.

First, in 1992, after searching for funds for several years (capital markets were very tight in the early 1990s), SCH raised $48 million ($43.5 million went to SoCal), giving in return both debt instruments that carried interest obligations and—what the new investors demanded—common stock. App. 6a, 61a-64a; App. 62a (quoting petitioner Doumani: "I knew of no sources that would lend us the money without any equity play"). The 1992 recapitalization put SoCal into regulatory compliance but sliced the original 1987 equity to become only a 50% stake in SCH; and, although that stake met "the Government's main concern" of maintaining petitioners' active participation, the Government terminated the RCMA. App. 7a, 63a.

Then, in 1995, as the 1989 legal changes were further phased in, SoCal needed still more new capital. This time, the sources of the new capital (roughly $60 million), who received both debt instruments carrying interest obligations and preferred stock carrying dividend obligations, also demanded complete equity ownership. *See* App. 66a ("[t]he

capital providers . . . would only agree to invest additional cash into SoCal if the Individual Plaintiffs' remaining ownership were extinguished"). As the Government noted below (U.S. Br. 30; U.S. Reply Br. 20), petitioners' 1987 equity had been rendered "worthless." Accordingly, "SCH *cancelled for no consideration the original shares issued to the Individual Plaintiffs* [petitioners]." App. 7a (emphasis added); *see* App. 67a-68a. The court of appeals summarized: "*As a result of this transaction, the ownership interest originally bargained for by the Individual Plaintiffs was extinguished.*" App. 7a (emphasis added); *see* App. 69a.[4]

3. Almost immediately, SoCal's condition improved, and by the end of 1996, "the institution was restored to a healthy capital position." App. 70a. "The effects of the Government's breach had thus been mitigated by the considerable efforts of the [I]nstitutional and Individual Plaintiffs and, of course, by the infusion of approximately $100 million in tangible capital. SoCal was finally out of the very deep hole it had been in for years." App. 70a, quoted at App. 8a. In 1998, SCH issued shares to the public in an Initial Public Offering, which established an objective market value. (By then, petitioners already had lost their 1987 equity stake.) Thereafter, SCH was merged into the holding company of another large California bank, and SoCal became part of the healthy California National Bank. App. 71a-72a. That is why the trial court concluded: "SoCal is a *Winstar* success story." App. 121a.

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[4] Petitioner Arbur, Inc., acquired a small *new* equity stake in the 1992 and 1995 recapitalizations. App. 6a-7a, 62a, 69a. That stake is not at issue in this petition, which concerns only compensation for loss of the 1987 equity—a loss that Arbur, Inc., incurred in common with the other petitioners. App. 74a.

B. Trial Court Proceedings

Petitioners, along with the thrift and its holding company, sued the United States for damages in the Court of Federal Claims. After years of joint proceedings with other *Winstar* cases, the court granted partial summary judgment finding liability in this case, App. 125a-75a, noting the parties' agreement that the transaction here was similar to the Statesman Savings transaction before this Court in *Winstar*. App. 141a. The court described the interrelated April 1987 agreements, focusing on the RCMA obligations. App. 143a-149a. It held "that the Government was a party to an express contract with SoCal, SCH, and the Individual Plaintiffs," which it referred to as the "Overall Contract." App. 149a. The court then noted the Government's concession that it breached its promise regarding the $217.5 million capital credit—a promise that, appearing in the RCMA, ran to petitioners as well as SoCal and SCH. App. 149a. The court also held that the Government breached its promise regarding goodwill. App. 150a-61a.

Subsequently, the court conducted an extensive trial and made detailed findings about the damages that the Institutional Plaintiffs (SoCal and SCH) and the Individual Plaintiffs (petitioners) separately suffered as a result of the Government's breach. App. 31a-124a. The court held that the Government's breach was a "'total breach'" within the meaning of *Mobil Oil*, 530 U.S. at 608 (quoting *Restatement (Second) of Contracts* § 243 (1979)). App. 52a-53a. The court found that the breach was the cause of SoCal's capital deficiency and consequent need to shrink and to change its business plans. App. 50a, 53a-59a. It specifically found that the breach caused the 1992 and 1995 recapitalizations of SCH, in which petitioners' 1987 equity was extinguished for no consideration as a condition of securing the new capital needed to keep SoCal in operation. App. 59a-62a, 66a-67a; *see* App. 61a ("the 1992 and 1995 recapitalizations would not

have been necessary in the absence of the Government's breach"), 65a ("principal cause of this additional [1995] round of capital raising"), 66a ("The capital providers . . . would only agree to invest additional cash into SoCal if the Individual Plaintiffs' remaining ownership interest were extinguished . . . ."). Noting that the FHLBB's approval of the 1987 transaction was expressly conditioned on the RCMA, to which petitioners were parties, the court found that "Secretary Simon and his fellow signatories' roles were not ancillary, as the Government urges, but rather central to this transaction. The thrift would have failed—and the acquisition never would have occurred—but for the Individual Plaintiffs." App. 101a-02a (citation omitted).

For the thrift and holding company, the trial court rejected several categories of damages (*e.g.*, lost profits) but awarded a total of $65,397,821.41 for specific excess costs (fees, higher costs of funds, etc.) that they would not have incurred had there been no breach. App. 87a-101a, 123a. The court awarded petitioners lesser damages, for different injuries. App. 101a-23a. Again rejecting several categories of claimed damages (App. 102a, 111a-18a), the court followed the damages analysis of *Bluebonnet Savings Bank, F.S.B. v. United States*, 266 F.3d 1348 (Fed. Cir. 2001), and held that petitioners were entitled to the equity stake they lost because of the Government's breach. App. 103a-04a. The court found that "the Government's breach was a substantial factor in the harm suffered, the complete loss of their [1987] ownership interest," and that this "harm was separate and distinct from that suffered by the Institutional Plaintiffs." App. 105a.[5] Moreover, the court expressly found that "*it was foreseeable*

[5] As the trial court noted, dilution of a shareholder's interests has been recognized to be, as a factual matter, a harm distinct from any harm to the corporation issuing the shares. *See Strougo v. Bassini*, 282 F.3d 162, 174-75 (2d Cir. 2002), cited at App. 105a. The Federal Circuit itself so held in *La Van v. United States*, 382 F.3d 1340, 1350 (Fed. Cir. 2004).

to the Government that new capital contributions to re-capitalize SoCal after the Government's breach would result in dilution and eventual extinguishment of the Individual Plaintiffs' ownership interest in SCH common equity." App. 106a (emphasis added).

The award for the Government-caused extinguishment of petitioners' 1987 equity (the "dilution damages"), based on expert testimony by Dr. Allan Kleidon of the University of Chicago, gave petitioners just part of what they would have had without the Government's breach. App. 106a-11a. It did not purport to be full compensation for "what might have been if there had been no breach": it did "not calculate the value of [petitioners'] share of SoCal in a non-breach world," and it did "not calculate or award any lost profits or share of lost profits to the thrift caused by the breach." App. 106a. Unlike the award to SoCal and SCH—which tried to bridge some of the difference between the *breached* thrift and the thrift without the breach—the award to petitioners "merely return[ed] to [petitioners] their share in the *breached* thrift" and did "not address or seek to address any increased value the thrift might have had" without the breach. App. 106a.

Had there been no breach, petitioners would have retained their 1987 equity past 1995. App. 107a. To measure the value lost, the court determined that petitioners' 1987 common stock would have represented 14.41% of the total common stock after SCH's 1998 Initial Public Offering (IPO), with each petitioner having an identified portion of that 14.41% (App. 108a-09a), and that the open-market IPO set an objective market value of $13.75 per share. App. 109a-10a. Multiplying that price per share by the number of shares that each petitioner would have owned in 1998, the court awarded damages totaling $28,671,573.75. App. 32a, 111a, 123a.[6]

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[6] The court of appeals mistakenly stated that the total damages to petitioners were $22,448,293.75. App. 9a. The court evidently read the trial

Having determined that such dilution damages were proper, the court rejected the Government's claims to offset the damages to petitioners and to deny such damages altogether for lack of mitigation. App. 118a-21a. The court found: "the Individual Plaintiffs acted reasonably and diligently, and in accordance with their contractual duties under the RCMA, to assure that SoCal was capital compliant." App. 120a.

C. The Court of Appeals Decision

A divided panel of the court of appeals reversed the award of damages to petitioners. App. 9a-22a. In so holding, the court did not question that the Government had breached its promise concerning the regulatory treatment of capital credits and supervisory goodwill. In fact, the court affirmed most of the damages to the Institutional Plaintiffs for that breach and remanded for further inquiry into one part of those damages. App. 22a-27a. (The Institutional Plaintiffs and Government have since settled.) In that context, the court recognized that damages raised a factual question of foreseeability. App. 25a. Nevertheless, when it came to petitioners, the majority held that there could be no recovery at all as a matter of law.

The court first concluded that petitioners were not parties to, and had no contract rights under, the Assistance Agreement, which named only the thrift and its holding company as private parties. App. 10a-19a. The court wholly disregarded the *FHLBB approval resolutions* themselves as conferring contractual rights on petitioners (the second question presented in this petition). In discussing the Assistance Agreement, under which it held that petitioners (shareholders of signatory SCH) had no rights, the court observed that corporate-veil-piercing standards generally protected against the *possibility* of double recovery by shareholders. App. 15a-

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court's statement that $6,223,280.00 was awarded to "both" Mr. Doumani and Mrs. Thrall (App. 32a) as meaning that they shared that amount, when in fact each was awarded that amount.

19a. The court did not say that there actually would be any double recovery in this case—the Government's briefs contain no such argument, reflecting the absence of such proof at trial—and the court raised no such concern when it turned to recovery for breach of the RCMA, to which petitioners were parties with their own contract rights.

The court expressly acknowledged that petitioners "were in contractual privity with the government under the RCMA." App. 19a. While noting that the trial court had not separately rested its damages award on breach of the RCMA alone (App. 15a n.4), the court of appeals entertained the obvious possibility that the RCMA breach itself caused the extinguishment of petitioners' 1987 equity for no consideration, then held that such damages were precluded as a matter of law. App. 19a-22a.[7] The primary question presented in this petition is the court's holding that ordinary expectation damages were legally barred.[8]

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[7] The court recognized that the RCMA promised that SoCal could count the $217.5 million in capital credits as regulatory capital. App. 19a, 20a ("incorporation of the capital credit promise into the terms of the RCMA"). SoCal had excess regulatory capital of $188 million before the 1989 legal changes that denied use of both the capital credits and the $79.5 million in supervisory goodwill (the latter addressed in the Board resolutions but not the RCMA). App. 51a. If only supervisory goodwill (phased out over several years) had been lost, and not the capital credits, SoCal would not have required the same level of new capital, if any at all. There is no finding or proof that the much smaller breach would still have caused extinguishment of petitioners' 1987 equity as the price for any much-reduced infusion of new capital.

[8] The damages at issue here are a form of expectation damages. The trial court erred in saying otherwise (App. 106a), when all it actually meant was that they do not claim the *full* expectation damages, *i.e.*, the *full* value of the lost equity if there had been no breach (*id.*): the damages represent only the value of the equity in the institution *as harmed by the breach* ("in the breached thrift"). *Id. Restatement* § 347 itself distinguishes several kinds of expectation damages. The court of appeals rightly did not judge

Critically, the court nowhere held clearly erroneous the trial court's factual findings that the Government breach caused the extinguishment of petitioners' 1987 equity and that such extinguishment was a foreseeable result of the breach (as the price of raising new capital needed after the breach). Nor did the court of appeals find that petitioners failed reasonably to mitigate their losses (or even address the issue). Rather, after reciting the usual foreseeability formulation, the court held as a matter of law that petitioners could not recover for destruction of their 1987 equity because the contract itself (the RCMA) did not require them to forfeit their equity and had not required their investment in the first place. App. 20a, 21a.

That rationale is set forth in two brief passages. First, speaking in unusual terms about damages' being caused by the harmed party's "obligations," rather than by the promisor's breach, the court said that the claim for damages under the RCMA failed to recognize that "*the damages for which the Individual Plaintiffs seek to recover, namely the dilution and extinguishment of their ownership interests in SCH, were not caused by the obligations they incurred in the RCMA.*" App. 20a (emphasis added). The problem here, the court immediately explained, was that "[t]he RCMA did not require that the Individual Plaintiffs invest in SCH." App. 20a.

After pointing to the usual three types of contract damages (expectation, reliance, restitution), and quoting the usual foreseeability standard for expectation damages, App. 20a-21a, the court returned to its reason for rejecting the damages under the RCMA as a matter of law. The court said: "*there are no terms in the RCMA that require the Individual Plaintiffs to raise capital for SCH and SoCal by diluting their ownership interest in order to issue equity to new investors.*"

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the availability of damages by binding itself or petitioners to the trial court's classification.

App. 21a (emphasis added). It then added that "[a]t the most" the RCMA obliged petitioners to contribute $5 million to achieve regulatory compliance (App. 21a), omitting mention of the other RCMA promises of forfeiture of stock to the Government if SoCal's capital fell too low or if petitioners' own equity fell below half. *See* pages 5-6, *supra*. On this sole basis ("Accordingly, based on the unambiguous terms of the RCMA")—that the RCMA did not itself mandate that petitioners would incur the loss of their 1987 equity—and with no *factual* inquiry into foreseeability or causation, the court held as a matter of law that petitioners' "loss of their ownership interests was neither the foreseeable result of nor caused by the government's breach of the RCMA." App. 21a. The court thus barred the expectation damages that would have partly restored petitioners to the position they would have occupied if the RCMA had been performed rather than breached.[9]

Judge Mayer dissented in part, disagreeing with the majority's rejection of petitioners' claims. App. 28a-30a. He explained that "[t]he RCMA is the basic contract document of the transaction" and concluded that the majority's rejection of a relief for petitioners "ignores the personal and individual contractual obligations that they assumed pursuant to the RCMA." App. 29a. In Judge Mayer's view, the trial court had correctly enforced the overall contract between petitioners and the Government. App. 29a-30a.

REASONS FOR GRANTING THE PETITION

Like the *Mobil Oil* case, this case calls for review to correct a Federal Circuit decision that abrogates for Government contracts the ordinary rules of commercial contract law. This

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[9] The court more sensibly discussed what actions petitioners did or did not take under the RCMA when discussing restitution, which concerns money contributed under a contract, and reliance, which concerns action taken in reliance on the promise made in the contract. App. 21a-22a.

Court held in *Mobil Oil*, following *Winstar* and other decisions, that rights under Government contracts are determined by following ordinary contract-law principles. Under those principles, petitioners are entitled to their factually foreseeable losses caused by the Government's breach of the bargained-for exchange that included the Government promises regarding regulatory capital. Yet the Federal Circuit, as in *Mobil Oil*, denied that elementary contract-law entitlement by departing from the standard principles of contract damages and of contract formation. This Court should grant review to make clear, once again, that such standard principles must be applied to Government contracts.

The primary legal question warranting review concerns the Federal Circuit's extraordinary limitation on contract damages. The Federal Circuit denied petitioners' damages claim for the destruction of their 1987 equity even though it did not question that petitioners had contract rights under the RCMA and did not question that the loss was as a factual matter foreseeable and caused by the Government's breach of the contract (and had been measured with reasonable certainty). Although it *recited* the usual foreseeability standard, the court rejected expectation damages as a matter of law by adding a novel limitation to that standard: that the contract itself must require the equity loss upon breach or the acquisition of the destroyed property in the first place.

The court's ruling violates the controlling law of contract damages, which entitles the harmed party to damages where they are foreseeable and caused as a factual matter. That entitlement gives effect to the bedrock contract-law principle that damages should give the harmed party what it would have had if the contract had been performed instead of breached—and here, petitioners' damages represent only a portion of that amount. The Federal Circuit cited no authority for its inventive limitation on contract damages, and the decision is a clear departure from other Federal Circuit decisions,

which repeatedly rely on the ordinary *factual* foreseeability standard. It is peculiarly important to correct the misguided limitation on government-contract damages adopted by the Federal Circuit, the appellate court with special authority over Government-contract claims, because the ruling will do substantial harm to the interests of both private parties and, ultimately, the Government itself.

The second legal question warranting review concerns what documents are part of the Government contract. The Federal Circuit, while accepting that the RCMA is certainly a contract between the Government and petitioners, rejected the trial court's finding that the overall contract was broader. Under basic contract-formation principles, the Bank Board approval resolutions themselves create contract rights, because, accepting petitioners' offer, they approved a financial transaction between the Government and petitioners and made promises to petitioners and imposed obligations on them as a condition of approval. The Federal Circuit, in disregarding the promises in the Bank Board resolutions, incorrectly narrowed the overall contract to the RCMA and thereby both stripped petitioners of part of their contract rights and created a conflict within the Circuit that is of unique importance on Government-contract issues. The Court should take this second question as well as the first to resolve the doctrinal confusion, to ensure proper protection of petitioners' rights, and to set straight the essential rules, about contract formation as well as damages, that govern financial dealings with the Government.

I. THE FEDERAL CIRCUIT'S RESTRICTION OF CONTRACT REMEDIES TO DENY RECOVERY FOR FORESEEABLE LOSS CAUSED BY BREACH SHOULD BE REVIEWED

A. The Decision Is Inconsistent With The Governing Law Of Contract Remedies

1. This Court has long made clear that the federal common law governing Government contracts is the general law of contracts governing private parties. *See, e.g., Mobil Oil*, 530 U.S. at 607 (quoting and adopting statement from *Lynch v. United States*, 292 U.S. 571, 579 (1934): "When the United States enters into contract relations, its rights and duties therein are governed generally by the law applicable to contracts between private individuals."); *Perry v. United States*, 294 U.S. 330, 352 (1935) ("When the United States, with constitutional authority, makes contracts, it has rights and incurs responsibilities similar to those of individuals who are parties to such instruments."); *Winstar*, 518 U.S. at 895 & n.39 (principal opinion, quoting *Perry*, *Lynch*, and other decisions); *Winstar*, 518 U.S. at 912 (Breyer, J., concurring) (quoting precedents). And the Court has repeatedly turned to the *Restatement (Second) of Contracts* for authoritative statements of general contract law. *See, e.g., Mobil Oil*, 530 U.S. at 608, 614, 621-22, 624 (relying on *Restatement* §§ 243, 250, 256-257, 373); *Winstar*, 518 U.S. at 863, 869-70, 886 n.30, 887 n.32, 895, 904-05, 907-08 (principal opinion) (relying on *Restatement* §§ 202, 261, 264, 346, 357-359).

The starting points of contract-remedy law are that "[e]very breach of contract gives the injured party a right to damages against the party in breach" (*id.* § 346 Comment a) and that the overarching purpose of contract damages is "to place the injured party in as good a position as he would have been in had the contract been performed" (*id.* ch. 16, Reporter's Note). The presumptive remedy protects the harmed party's expectation interest. "Ordinarily, when a court concludes that

there has been a breach of contract, it enforces the broken promise by protecting the expectation that the injured party had when he made the contract." *Id.* § 344 Comment a; *id.* § 347. And the scope of the expectation damages is presumptively broad: they are "measured by (a) the loss in the value to him of the other party's performance caused by its failure or deficiency, plus (b) any other loss, including incidental or consequential loss, caused by the breach, less (c) any cost or other loss that he has avoided by not having to perform." *Id.* § 347. The intent is to give the harmed party "the benefit of his bargain by awarding him a sum of money that will, to the extent possible, put him in as good a position as he would have been in had the contract been performed." *Id.* § 347 Comment a.

Consequently, as § 347(b) particularly indicates, "the injured party is entitled to recover for all loss actually suffered" (*id.* § 347, Comment c)—subject only to certain limitations stated in §§ 350-353. The limitation relevant to this petition is stated in § 351: "Damages are not recoverable for loss that the party in breach *did not have reason to foresee* as a probable result of the breach when the contract was made." (Emphasis added.) With this limitation, damages caused by breach, if "foreseeable," are recoverable. *Id.* Comment a.

Foreseeable damages, including incidental and consequential damages, are *not* limited to losses required by, or even addressed in, the contract, let alone losses of property acquired under the contract. "[T]he party in breach need not have made a 'tacit agreement' to be liable for the loss. Nor must he have had the loss in mind when making the contract, for the test is an objective one based on what he had reason to foresee." *Id.* The recoverable losses include "general" damages, *i.e.*, those which result from breach in the ordinary course of events, and also "special" damages, *i.e.*, those which the breaching party "had reason to know" of when contracting—a premise that is "*sometimes* established by the

use of recitals in the agreement itself," but need not be. *Id.* Comment b (emphasis added). Recoverable costs need only be foreseeable, not foreseen, let alone expressly foreseen. *See Fidelity & Deposit Co. v. Krebs Engineers*, 859 F.2d 501, 507 (7th Cir. 1988) ("The test for recovering consequential damages is not whether the seller actually foresaw or contemplated the resulting damages when it made the contract; instead, the test is whether the seller, knowing or having reason to know the buyer's needs, could have reasonably foreseen the loss as a probable consequence of a breach."). The point is confirmed by the contrast with *reliance* damages, which focus on compensating for expenditures made pursuant to the contract (*Restatement* §§ 344(b), 349), whereas *expectation* damages do not.

2. The Federal Circuit decision in this case violates those straightforward principles. Although the Federal Circuit articulated the foreseeability standard for expectation damages in its paragraph reciting the basic principles of contract damages, App. 20a-21a, it radically tightened the standard when it gave its sole reason for reversing the trial court's finding of such damages. Simply, the decision rejects damages for the extinguishment of petitioners' 1987 equity either because the RCMA itself did not require petitioners to incur the loss of their 1987 equity or (what the court might have thought the same point or a different point) because the contract did not require petitioners to acquire the 1987 equity in the first place. App. 20a, 21a.

That ruling is contrary to the governing law. If a loss to a non-breaching party is foreseeable as a matter of fact, it does not become unforeseeable as a matter of law simply because it is not specifically required by the contract or because the property lost had been acquired before the contract was formed. The basic principle of contract damages, applicable to Government contracts under this Court's decisions, is that the breaching party is liable for any foreseeable loss, whether

or not it is specifically addressed in the contract. The Federal Circuit's holding cuts a significant hole in that guarantee of recoverable damages. In fact, it effectively reinstates, for damages, the very requirement of a "second promise" that was rejected, for liability, in *Winstar*. 518 U.S. at 887 (principal opinion); *id.* at 921 (Scalia, Kennedy, Thomas, JJ., concurring in the judgment).

Importantly, the Federal Circuit nowhere questioned as a *factual* matter the trial-court finding that the loss of the 1987 equity was a foreseeable consequence of the Government's breach of its regulatory-capital contract. Nor could it have done so. It was foreseeable that, without the regulatory-capital treatment promised by the Government, more capital would have to be raised. (The Federal Circuit noted that one of the very reasons for that treatment in 1987 was to "eliminat[e] the need for the acquiring thrift[] to obtain additional capital infusions." App. 4a.) It was predictable that investors supplying such new capital, to a business teetering on the brink of failure, would demand receipt of the upside potential of the business, indeed complete equity ownership and control, as an offset to the grave risk they were assuming. *See* App. 66a (the 1995 "capital providers . . . would only agree to invest additional cash into SoCal if the Individual Plaintiffs' remaining ownership interest were extinguished"). Factually, then, it was foreseeable that loss of the original equity would be the price of raising the capital that would be needed upon Government breach.

Indeed, it was foreseeable that the value of petitioners' 1987 equity would be driven to zero by breach of the Government's regulatory-capital commitment. When new investors demanded cancellation of that destroyed equity, it was foreseeable that cancellation would occur without consideration. And it was foreseeable that these particular investors—on whose personal probity and reputations the Government was expressly relying—would follow through on their commit-

ment to help the thrift thrive, even at the cost of their 1987 equity, already destroyed in value by the breach. Finally, what petitioners lost was itself known by the Government to be bound up with the very creation of the contract: the RCMA required petitioners to *maintain* a majority equity stake and provided for forfeitures of the equity stake if capital became insufficient; as the court of appeals recognized, SCH's (and hence petitioners') acquisition of SoCal, with all its risks, was conditional on the required Government approval, which was expressly conditional on the RCMA; and SCH itself was formed just months earlier solely to acquire SoCal. *See* pages 3, 6, & n.2, *supra*

In these circumstances, the Federal Circuit could not have reversed the trial court's finding on foreseeability as a factual matter. Its reversal of damages thus necessarily relied on its articulated limitation on contract damages. Because that limitation is of dispositive significance here, and contrary to governing law that is vital to a just contract-damages regime, this case is a good vehicle for this Court's review.

B. The Decision Creates Lower Court Doctrinal Conflicts

The Federal Circuit decision creates conflicts over fundamental principles of contract-remedy law where it most matters for Government contracts. Even Federal Circuit decisions that directly concern the *Winstar* situation conflict with the decision below. So, too, do non-*Winstar* decisions.

In *Bluebonnet*, an investor, James Fail, rescued a FSLIC-insured thrift: through a Capital Maintenance Agreement and other agreements with FSLIC, Fail's company, CFSB, purchased the stock of the thrift, Bluebonnet Savings Bank. 266 F.3d at 1351. After the Government breached its regulatory-capital promises, Fail was forced to give up 49% of his interest in CFSB so that the thrift could obtain the money it needed by law. *Id.* at 1354 (describing "Economic Benefits

Agreement," or EBA). In the suit by "Bluebonnet"—the thrift, the holding company (CFSB), *and* Fail (*id.* at 1350)—the Federal Circuit held that damages were available and remanded for calculation. *Id.* at 1355-58. Invoking *Restatement* §§ 344, 347, 351, 352, the court ruled that "[e]xpectation damages are recoverable provided they are actually foreseen *or reasonably foreseeable*, are caused by the breach of the promisor, and are proved with reasonable certainty," with "[f]oreseeability . . . a question of fact reviewed for clear error." 266 F.3d at 1355 (emphasis added). And the court held that damages *were* available in circumstances closely akin to this case, with no further demand that the contract itself address the losses at issue, contrary to the demand of the panel in this case.[10] The *Bluebonnet* decision contradicts the decision in this case, notwithstanding the present decision's bow to the general standard from *Bluebonnet* (App. 20a).

The decision below also conflicts with the Federal Circuit decision in *La Van*, *supra*, which likewise involved facts

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[10] The Federal Circuit first affirmed the district court's finding that it was foreseeable that breach of the regulatory-capital promises would require raising new capital at higher cost (*id.* at 1356), which included as part of the "damages claimed" the 49% dilution of Fail's equity interest in the thrift's holding company (CFSB) that was part of "the cost of the EBA" (*id.* at 1356). The Federal Circuit then reversed the district court's finding that the EBA cost was not caused by the Government breach. The Federal Circuit explained that "[t]he EBA, and its grant of a 50 percent equity stake in CFSB . . ., was only entered into because the breach removed" the otherwise-available "source of funds for the required capital infusions" and that "[i]n the absence of the breach, Fail and CFSB would not have agreed to the EBA . . . and it would have been unnecessary to give up a significant equity stake in CFSB to obtain financing." *Id.* With the clearly erroneous non-causation finding reversed, the Federal Circuit "remanded with instructions to formulate an appropriate award of EBA-related damages as determined by [certain payments already made] and the value of the EBA debt as calculated [in a specified document]." *Id.* at 1358.

similar to this case. After finding a contract between the FHLBB and a thrift's investors, and breach of the regulatory-capital promise, 382 F.3d at 1346-49, the court in *La Van* held that the investors suffered damages distinct from those suffered by the thrift, that the investors were entitled to expectation damages (the claim was for loss in value of their stock), and that the standard for damages was the usual make-whole principle based on foreseeability. *Id.* at 1349-51. That holding cannot reasonably be squared with the decision in this case—which is inconsistent with principles reflected in other *Winstar* cases, too. *See Home Savings of America v. United States*, 399 F.3d 1341, 1347, 1355 (Fed. Cir. 2005) ("[i]n contract cases, causation, foreseeability, and certainty [of damages] are questions of fact reviewed for clear error"; finding that need for new capital and costs of raising it were a foreseeable result of breach of FHLBB regulatory-capital promises); *see also Landmark Land Co. v. FDIC*, 256 F.3d 1365 (Fed. Cir. 2001) (following *Restatement* and factual foreseeability standards in restitution context).

More generally, outside the *Winstar* setting the Federal Circuit and its predecessor Court of Claims have long recognized that contract damages are recoverable when, as a factual matter, they are reasonably foreseeable, without separate legal limitation to costs promised under the contract whose breach caused the damages. *See, e.g., Indiana Michigan Power Co. v. United* States, 422 F.3d 1369, 1373 (Fed. Cir. 2005); *Prudential Ins. Co. of America v. United States*, 801 F.2d 1295, 1300 (Fed. Cir. 1986); *Northern Helex Co. v. United States*, 524 F.2d 707, 714-15, 720-21 (Ct. Cl. 1975). The General Services Board of Contract Appeals applies the foreseeability standard of *Restatement* § 351 as well. *See Data Enters. of the Northwest v. GSA*, 2004 WL 323922 (GSBCA No. 15607). The decision in this case, in adding a new limitation, leaves the governing damages standards in conflict and confusion.

C. It Is Important To Correct This Decision By The Appellate Court With Special Authority Over Government Contracts

Federal Circuit precedent is uniquely important to the law governing Government contracts. That circuit has exclusive appellate jurisdiction in contract damages cases against the Government, whether brought originally in the Court of Federal Claims or in district court, as well as over appeals (by the contractor *or* the Government) under the Contract Disputes Act. 28 U.S.C. §§ 1295(a)(2) & (3), 1295(a)(10), 1346(a)(2), 1491(a)(1). Accordingly, significant errors, inconsistencies, or uncertainties in the Federal Circuit's precedents on Government contract law are specially harmful and need review. Government contractors and the Government itself will have their contracting behavior, and their ability to secure proper remedies, uniquely affected by errant or unclear Federal Circuit precedent.

The availability and scope of contract remedies are of the most pervasive possible significance to contracting parties. On this crucial matter, the doctrinal inconsistency created by the decision in this case necessarily leaves parties to Government contracts uncertain. And the extraordinary limitation on contract damages articulated and applied to deny petitioners relief in this case, if allowed to stand, will do continuing harm both to contractors and to the Government itself.

One source of harm is the injustice of denying relief for a proven harm caused by the Government's breach. It has long been recognized that "damages are always the default remedy for breach of contract." *Winstar*, 518 U.S. at 885 & n.30 (principal opinion). And that principle serves well-recognized interests in market efficiency, which will be harmed by the Federal Circuit's novel constriction of expectation damages.

An additional, systemic harm from the precedent this decision establishes for denying such relief—harm to the interests of the Government itself—is made evident by the discussion

of a closely related context in the principal opinion in *Winstar*, 518 U.S. at 883-85. Stripping private parties of their remedies for foreseeable harm, like the broad invocation of "unmistakability doctrine" to limit contract enforcement, would place federal contract law "at odds with the Government's own long-run interest as a reliable contracting partner in the myriad workaday transaction of its agencies." *Id.* at 883. Private parties, when contracting, would have to incur the substantial expense of trying to anticipate all foreseeable consequences and negotiate terms to cover them, fostering the very inefficiencies that sound principles of contract-remedy law avoid. *Id.* at 884 & n.27. The Federal Circuit decision here, if not reversed, thus would "produce the untoward result of compromising the Government's practical capacity to make contracts," if only by "increasing the cost of its engagements." *Id.*

The Government could easily be harmed by the Federal Circuit's legal principle in yet another way. The Federal Circuit did not purport to state a one-way limitation that would restrict only private claimants' rights against the Government; and any such stark asymmetry would in any event be unsustainable, as the principal opinion explained in *Winstar*, 518 U.S. at 886 & n.31. The limitation on contract remedies, therefore, would have to apply when the Government itself sought damages for breach of a Government contract. The ruling in this case thus threatens the interests of the Government even as a potential contract claimant, further adding to the reasons for review.

II. THE FEDERAL CIRCUIT'S REJECTION OF CONTRACT RIGHTS BASED ON THE BANK BOARD'S APPROVAL RESOLUTIONS SHOULD BE REVIEWED

The Federal Circuit's decision departs in a second way from the ordinary principles of commercial contract law that this Court has held to control Government contracts. Al-

though the Federal Circuit's rejection of damages for petitioners is wrong and worthy of review even if the sole contract at issue is the RCMA, which the Federal Circuit expressly recognized to be a contract between petitioners and the Government, the Federal Circuit also took too narrow a view of the source of petitioners' contract rights. It should have recognized that the FHLBB resolutions approving the 1987 SoCal transaction themselves created contract rights for petitioners. The trial court held that those resolutions were part of an overall contract between petitioners and the Government. Yet the Federal Circuit, which focused only on the Assistance Agreement (which it found did not give petitioners contract rights) and the RCMA (which it found did), wholly disregarded the Bank Board resolutions as part of the overall contract. In doing so, it committed an error that is important to correct.[11]

The principal Bank Board resolution directly and repeatedly addresses petitioners. It refers to "the bid of the Investors [*i.e.*, petitioners] to acquire" the thrift, App. 197a, and to "the offer of the Investors" (App. 215a), that prompted the approval resolutions. It approves the negotiated financial transaction involving FSLIC, petitioners (whom it gives special permission for the transaction), and the thrift and its holding company—a transaction financially benefiting the Government (lessening the risk to FSLIC). As a condition of such approval, it imposes specific obligations on petitioners,

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[11] This issue has the following practical significance in this case. A reversal on the RCMA damages alone would leave for remand the question whether the damages were caused by repudiation of the RCMA's capital-credit promise. Although the answer "yes" should readily be given, further litigation over that question would be avoided if this Court also clarified that the FHLBB resolutions, which contain the promise regarding goodwill as well as capital credits, were part of the Board's contract. In that event, the trial court's finding that the loss of the 1987 equity was caused by the breach of both government promises would stand.

including their execution of the RCMA, which petitioners simultaneously did. And it specifically provides for the goodwill and capital-credit regulatory treatment that was essential for the private investments to make economic sense. *See* page 6, *supra* (reciting specifics of resolutions).

In these circumstances, the Bank Board resolutions were themselves part of a bargained-for exchange of promises and performances, with offer and acceptance, that suffice to make a contract. *See Restatement* §§ 17-24, 50, 71-72. Indeed, in *Winstar*, the principal opinion explained that, even aside from any incorporation of Board approval resolutions by a separate document signed by the parties, the circumstances made clear that the approval resolutions were enforceable contracts. 518 U.S. at 863-64; *see id.* at 919 (Scalia, Kennedy, Thomas, JJ., concurring in the judgment). The same conclusion is required here: as the trial court properly held, the full regulatory-capital treatment promised in the Board approval resolutions is part of the contract petitioners are entitled to enforce. *See* App. 38a-42a, 44a. The contrary decision by the Federal Circuit is contrary to familiar contract-formation law.

The decision also creates intra-circuit conflicts in this very context. In *Home Savings*, the Federal Circuit held that the thrift's holding company, Ahmanson, *though not a signatory to the Assistance Agreements*, had enforceable contractual rights against the Government. Pointing to the fact that Ahmanson had been "the offeror that initiated the negotiations" with the Government, the court held that the FHLBB approval resolutions were an enforceable contract because they contained "reciprocal promises that were part of the overall bargains between" the thrift, its owner Ahmanson, and the Government. 399 F.3d at 1349-50. The same is true here. Although the details of the promises differ in the two cases—Ahmanson apparently obligated itself outright to maintain the thrift's net worth, while petitioners made more limited though closely related promises—the details do not alter the material

point: the FHLBB resolutions approving the financial transaction, in addressing particular persons and imposing certain obligations on them, themselves were part of an enforceable contract. The contract, here and in *Home Savings*, included the full FHLBB-articulated promises regarding regulatory-capital accounting.

The decision below also conflicts with the decision in *La Van*, *supra*. There, the Federal Circuit held, with no reference to any other agreement by the parties, that Bank Board resolutions—which addressed the capital-supplying investors, reflected negotiations and a bargained exchange with them, and made the regulatory promise regarding goodwill—themselves constituted an enforceable contract with the investors in the rescued thrift. 382 F.3d at 1346-49. The same conclusion should follow here. *See also California Fed. Bank, FSB v. United States*, 245 F.3d 1342, 1346-47 (Fed. Cir. 2001) (Board resolutions and letters create contract even without additional signed agreement); *Cain v. United States*, 350 F.3d 1309, 1317 (Fed. Cir. 2003) (Newman, J., dissenting).

These *Winstar*-specific conflicts are reason enough for review, but the conflict is in fact more general. The decision below unsettles the previously established precedents that state more generally "'the requirements for a contract with the Government . . . : mutual intent to contract including an offer and acceptance, consideration, and a Government representative who had actual authority to bind the Government.'" *California Fed. Bank*, 245 F.3d at 1346 (quoting *Massie v. United States*, 166 F.3d 1184, 1188 (Fed. Cir. 1999), and *Trauma Serv. Group v. United States*, 104 F.3d 1321, 1326 (Fed. Cir. 1997)). Those elements are present here: a bid by petitioners, acceptance by the Bank Board exercising its authority, imposition of obligations on petitioners in exchange for Board promises in the approval resolutions. Yet the Federal Circuit rejected the trial court's treatment of the Board resolutions as part of the contract.

This Court should grant review on this issue as well as the first question presented in this petition. Which Government pronouncements and actions give rise to contract rights is fundamental to contract law (and parties' behavior in reliance on their understanding of such law), and the Federal Circuit is uniquely important in addressing that subject, given its exclusive appellate jurisdiction in the area. Intra-circuit confusion is now apparent on this matter. Extending the grant of certiorari to this issue would allow for resolution of the confusion and for restoration of the previously established, sensible standards governing contract formation.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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March 21, 2006

APPENDIX

APPENDIX A

UNITED STATES COURT OF APPEALS
FEDERAL CIRCUIT

Nos. 04-5036, 04-5038

SOUTHERN CALIFORNIA FEDERAL SAVINGS & LOAN ASSOCIATION AND SOCAL HOLDINGS, INC.,
Plaintiffs-Appellees,

and

ARBUR, INC., WILLIAM E. SIMON, JR., J. PETER SIMON, and GEORGE J. GILLESPIE, III
(Executors of the Estate of William E. Simon, Sr.),
Plaintiffs-Appellees,

and

ROY DOUMANI, PRESTON MARTIN, AND BEVERLY W. THRALL
(Successor to the Claims of Larry B. Thrall),
Plaintiffs-Cross Appellants,

v.

UNITED STATES,
Defendant-Appellant.

Aug. 22, 2005
Corrected Aug. 30, 2005
Rehearing and Rehearing En Banc Denied Dec. 27, 2005.

Before NEWMAN, MAYER and GAJARSA, *Circuit Judges*.

Opinion for the court filed by Circuit Judge GAJARSA. Dissenting opinion filed by Circuit Judge MAYER.

GAJARSA, *Circuit Judge*.

The United States appeals two decisions made by the Court of Federal Claims in this *Winstar*-related case. First, it challenges the court's grant of summary judgment finding the government liable for breach of contract to Arbur, Inc., the Estate of William E. Simon, Sr. (collectively, the "Simon Plaintiffs") and Roy Doumani, Preston Martin, and Beverly W. Thrall (collectively, the "DMT Plaintiffs"). *Southern Calif. Fed. Savings & Loan Assoc. v. United States*, 52 Fed.Cl. 531 (2002) ("*SoCal I*"). Second, the government challenges the amount and propriety of damages awarded after trial to Southern California Federal Savings & Loan Association and SoCal Holdings, Inc. (collectively, "the Institutional Plaintiffs") as well as the damages awarded to the Simon Plaintiffs and the DMT Plaintiffs (collectively, the "Individual Plaintiffs"). *Southern Calif. Fed. Savings & Loan Assoc. v. United States*, 57 Fed.Cl. 598 (2003) ("*SoCal II*"). The DMT Plaintiffs cross-appeal the court's refusal to award them additional damages based on the government's proposed cost of mitigation. *Id.* at 641. Because the Court of Federal Claims erred in holding that the Individual Plaintiffs have standing to sue for breach of contract, we vacate the court's judgment finding the government liable to them and awarding them damages based on that liability. Although we agree that the Institutional Plaintiffs are entitled to the categories of damages awarded to them, there are issues with the calculation of those damages that require further fact-finding to fully resolve. Accordingly, we affirm in part and reverse in part the court's award of damages to the Institutional Plaintiffs and remand for further proceedings.

I. BACKGROUND

A. Overview of *Winstar* Litigation

This is a *Winstar*-related case involving claims against the government stemming from Congress' enactment of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), Pub.L. 101-73. FIRREA was

passed as part of the government's response to the savings and loan crisis of the 1980s. *Castle v. United States*, 301 F.3d 1328, 1332 (Fed.Cir.2002). The circumstances surrounding the crisis in the savings and loan industry are well-documented elsewhere, *United States v. Winstar Corp.*, 518 U.S. 839, 843-58 (1996), and therefore we need not recount them in detail here. An understanding of the government's response to that crisis and the resulting litigation is, however, helpful to appreciating the issues raised by this case, so we begin with a brief overview.

The rise of interest rates in the 1980s caused a number of savings and loan institutions, or thrifts, to become insolvent when the interest rates they were required to pay on new deposits exceeded the income generated from existing mortgages entered into at lower rates. *Castle*, 301 F.3d at 1332. In response, the agency that insured thrift deposits, the Federal Savings and Loan Insurance Corporation ("FSLIC"), and the regulator of all federally insured thrifts, the Federal Home Loan Bank Board ("FHLBB"), sought private investors and healthy thrifts to take over ailing thrifts. *Id.* As an incentive to engage in such mergers, the FSLIC and the FHLBB routinely agreed to afford the acquiring thrifts particular regulatory treatment. *Id.* at 1333.

A commonly contracted for benefit involved the treatment of "supervisory goodwill." Supervisory goodwill was generated by the excess between an ailing thrift's liabilities assumed by an acquirer and the fair value of its identifiable assets. *Winstar Corp. v. United States*, 64 F.3d 1531, 1536 (Fed.Cir.1995) (en banc). The FHLBB permitted the acquiring thrifts to count supervisory goodwill toward the thrift's regulatory capital requirements, despite contrary teachings under generally accepted accounting principles ("GAAP"). *Castle*, 301 F.3d at 1333. This treatment of supervisory goodwill facilitated satisfaction of the regulatory capital

requirements by minimizing or eliminating the need for the acquiring thrifts to obtain additional capital infusions. *Id.*

The FHLBB and the FSLIC also used a capital credits incentive to encourage mergers with failing thrifts. The capital credits incentive involved FSLIC making a cash contribution to the merged thrift, which contribution could then be accounted for in partial satisfaction of the merged thrift's regulatory capital requirements. *Winstar Corp.*, 64 F.3d at 1536.

FIRREA, which was enacted in 1989, required, among other things, that thrifts maintain core capital of at least three percent of their total assets, and prohibited counting unidentifiable intangible assets, such as supervisory goodwill, toward this capital maintenance requirement. *Id.* Although the statute did not directly address the treatment of capital credits, concomitant regulations required that capital credits be treated in the same manner as supervisory goodwill. *Winstar*, 64 F.3d at 1538. As a result of the passage of FIRREA and the promulgation of related regulations, many thrifts that were previously in full compliance with the regulations on capital requirements failed to satisfy the new capital standards and immediately became subject to seizure. *Id.* Thus, the *Winstar* litigation was spawned whereby acquirers of the failing thrifts alleged that the government's enactment and implementation of FIRREA constituted a breach of the contracts promising thrifts particular regulatory treatment. *Castle*, 301 F.3d at 1333.

B. The SoCal Transaction

In 1986, the Individual Plaintiffs[1] responded to the government's solicitation of purchasers for the failing Southern

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[1] In addition to the Individual Plaintiffs, Gerald L. Parsky was also a significant investor in SCH and the purchase of Old Southern. *Southern Calif. Fed. Savings & Loan Ass'n v. United States*, 52 Fed.Cl. 444, 447 (2002). For unexplained reasons, Parsky was not a party to the com-

California Savings and Loan Association ("Old Southern"). *SoCal I*, 52 Fed.Cl. at 545. The Individual Plaintiffs proposed to form and personally capitalize a holding company to be named SoCal Holdings, Inc. ("SCH"). *Id.* SCH would in turn purchase Old Southern and form a new savings and loan association. *Id.* Upon government approval, the new association, a wholly-owned subsidiary of SCH named Southern California Federal Savings and Loan Association ("SoCal"), would acquire all the assets and liabilities of Old Southern. *Id.* at 546. The government approved the acquisition proposal and, on April 30, 1987, a series of agreements were entered into to complete the transaction. Three of those agreements/documents are most relevant to the current litigation. The Assistance Agreement was the primary document governing the transaction and it was entered into by SCH, as the acquirer of Old Southern, SoCal, and FSLIC. In conjunction with the execution of the Assistance Agreement, the FHLBB issued a Forbearance Letter addressed to Preston Martin as Chairman of the Board and Chief Executive Officer of SCH. The Forbearance Letter included the FHLBB's promise that SoCal could depart from GAAP in accounting for its capital credits and its supervisory goodwill. Finally, the Regulatory Capital Maintenance Agreement ("RCMA") was entered into by SCH, the Individual Plaintiffs, SoCal, and the FSLIC. Section 1 of the RCMA required SCH to maintain the regulatory capital of SoCal at the level specified by the applicable regulations and stated that the FSLIC capital credit would be includable as capital in order to meet that requirement. The RCMA also obligated the Individual Plaintiffs to "guarantee the performance of [SHC] and [SoCal] under § 1, provided that . . . the personal obligations of the [Individual Plaintiffs] under

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plaints filed in this action. *Id.* Parsky's attempts to file a separate claim were dismissed as time-barred. *Id.* at 448. The absence of Parsky is not material to this action.

said guarantees shall not exceed $5,000,000 in the aggregate." Execution of the RCMA was an express condition to FSLIC's obligations under the Assistance Agreement.

By 1989, SoCal's financial situation had improved greatly. *SoCal II*, 57 Fed.Cl. at 607. Its MACRO/CAMEL rating[2] had moved from a 4 to a 3. *Id.* Despite a tightening of the market, a decline in mortgage originations, and increased competition from other California thrifts, SoCal had grown from approximately $900 million at the time of the acquisition by SCH to approximately $2.3 billion by 1989. *Id.*

With the changes in capital requirements wrought by FIRREA, SoCal became a troubled institution. *Id.* at 608. After FIRREA took effect, SoCal's capital ratio dropped to 1.45%, substantially below its regulatory capital requirement, and its MACRO/CAMEL rating was dropped to a 4. *Id.* at 609. The Court of Federal Claims found that the drop in SoCal's regulatory capital negatively affected SoCal's retail and wholesale customer base, its long-term strategic plans, and its cost of acquiring operation capital. *Id.* at 610.

In an effort to comply with FIRREA, SoCal disposed of assets, which meant that it required less capital as a percentage of assets. *Id.* at 612. The thrift could not shrink fast enough, however, so it was forced to raise additional capital to become compliant. *Id.* In 1992, SCH issued $48 million in senior debt to Arbur, Inc. and two new investors. *Id.* at 614.

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[2] Federal regulators rate thrifts according to the effectiveness of their management and the Board of Directors, their asset quality, capital adequacy, asset/liability and risk management, and earnings (operations). *SoCal II*, 57 Fed.Cl. at 605. Prior to FIRREA, the rating system was denominated by the anagram MACRO and after FIRREA, the anagram CAMEL (capital, assets, management, earnings, liability) was used. *Id.* Using a scale of 1-5, with 1 being the highest rating and 5 being the lowest, the MACRO/CAMEL rating is considered an accurate description of the condition of a thrift at a given point in time. *Id.* at 607.

In addition to receiving interest payments, Arbur and the new investors received shares of a newly-created Class A common stock and the original common stock, which previously had no class designation, was converted to Class B common stock. *Id.* The effect of the 1992 recapitalization was to dilute the ownership of the Individual Plaintiffs from 100% of the common stock before the transaction to 51.36% after the transaction. *Id.* The 1992 recapitalization brought SoCal into compliance under the FIRREA capital standards and raised its MACRO/CAMEL rating to a 3. *Id.* at 615. Following the consummation of this transaction, the government terminated the RCMA. *Id.*

By November 1994, SoCal was again on the brink of failure, having been assigned a MACRO/CAMEL rating of 5. *Id.* at 616. The Court of Federal Claims found that SoCal's troubles were principally caused by FIRREA, in part because of the increasingly stringent capital requirements imposed as the act went fully into effect. *Id.* at 615. A second re-capitalization was executed in June 1995, with the 1992 capital providers as the sole participating entities. *Id.* at 617. The senior notes issued in 1992 were returned to SCH and contributed to the capital of SoCal. *Id.* Additionally, the two outside investors from 1992 purchased $10 million in new debt, with an increasing interest rate. *Id.* SCH also issued a $2 million senior note to Arbur, Inc. *Id.* In equity, SCH cancelled for no consideration the original shares issued to the Individual Plaintiffs and exchanged the preferred stock issued in 1992 for common stock. *Id.* Finally, SCH issued three new series of preferred stock to the 1992 investors, of which all three series required quarterly dividend payments. *Id.* For the equity, SCH received $48.5 million. *Id.* As a result of this transaction, the ownership interest originally bargained for by the Individual Plaintiffs was extinguished. *Id.*

After the 1995 recapitalization, the health of SoCal gradually improved. The Court of Federal Claims found that as of December 31, 1996, "[t]he effects of the Government's breach had thus been mitigated by the considerable efforts of the Institutional and Individual Plaintiffs and, of course, by the infusion of approximately $100 million in tangible capital. SoCal was finally out of the very deep hole it had been in for years." *Id.* at 618.

C. Proceedings Before the Court of Federal Claims

The Institutional Plaintiffs and the Individual Plaintiffs filed suit in the Court of Federal Claims to recover damages they incurred by the enactment of FIRREA. In *SoCal I*, the court addressed issues of the government's liability. In response to a summary judgment motion on behalf of all the plaintiffs, the government admitted that it had an express contract with the Institutional Plaintiffs, but argued that the Individual Plaintiffs lacked standing because they did not have privity of contract. *SoCal I*, 52 Fed.Cl. at 541. The court found that the government's execution of the Assistance Agreement, the RCMA and the FHLBB implementing resolutions all on the same day evidenced its intent to contract with all the plaintiffs. *Id.* at 542. Interpreting the merger clause of the Assistance Agreement to support this conclusion, the court found that the transactional documents created one overall contract to which the Individual Plaintiffs, as well as the Institutional Plaintiffs, were party. *Id.* at 543. Accordingly, the court held that the Individual Plaintiffs had standing to sue and granted the plaintiffs' summary judgment motion finding the government liable for breach of the overall contract. *Id.* at 549.

After a two month trial, the Court of Federal Claims issued an opinion awarding damages to the plaintiffs. The court awarded the Institutional Plaintiffs a total of $65,397,821.41 for "wounded bank" damages and "cost of replacement capital" damages. *SoCal II*, 57 Fed.Cl. at 601. Wounded

bank damages, which the court classified as a type of reliance damages, compensate for the costs incurred by the thrift because of its status as a "troubled" or under-capitalized institution. *Id.* at 624. Such costs include higher costs of funds, higher insurance and regulatory premiums and assessments, and extra attorney and consultant fees to interface with the regulators. *Id.* Damages for cost of replacement capital, which the court also classified as a form of reliance damages, compensate for the money spent by the thrift to replace the goodwill lost as a result of the government's breach. *Id.* In regards to the Individual Plaintiffs, the Court of Federal Claims awarded a total of $22,448,293.75 in "dilution damages". *Id.* at 601. Under the dilution theory, which the court classified as a form of restitution damages, *id.* at 623, the Individual Plaintiffs were awarded either the value of the breached thrift at a given point in time or a dollar amount corresponding with the cost of replacing their equity in the breached thrift, *id.* at 634.

Final judgment in the case was entered on September 10, 2003. The government filed a timely Notice of Appeal and now challenges the holding that the Individual Plaintiffs have standing to sue and the amount of damages awarded to both the Individual Plaintiffs and the Institutional Plaintiffs. This court has jurisdiction pursuant to 28 U.S.C. § 1295(a)(3).

II. DISCUSSION

This court reviews the Court of Federal Claims' grant of summary judgment under a de novo standard of review. *Winstar*, 64 F.3d at 1539. Whether a plaintiff has standing to bring suit is likewise a question of law, reviewed de novo. *Consol. Edison Co. v. Richardson*, 233 F.3d 1376, 1379 (Fed. Cir.2000). Standing is a threshold jurisdictional issue that

implicates Article III of the Constitution.[3] *Castle*, 301 F.3d at 1336.

The existence or non-existence of a contract is a mixed question of law and fact; contract interpretation is a question of law, reviewed de novo. *Id.* Questions regarding whether a breach of contract caused certain damages are questions of fact reviewed under the clear error standard. *Bluebonnet Savings Bank, F.S.B. v. United States*, 266 F.3d 1348, 1356 (Fed.Cir.2001). A finding is clearly erroneous when, despite some supporting evidence, "the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." *United States v. U.S. Gypsum Co.*, 333 U.S. 364, 395 (1948).

A. Standing of the Individual Plaintiffs

A plaintiff must be in privity with the United States to have standing to sue the sovereign on a contract claim. *Anderson v. United States*, 344 F.3d 1343, 1351 (Fed.Cir.2003); *see also United States v. Algoma Lumber Co.*, 305 U.S. 415, 421 (1939) (declining to presume that the government's actions gave rise to contractual obligations when the government was not a named party to the contract in suit). Not only is privity a fundamental requirement of contract law, but it takes on even greater significance in cases such as this, because the "government consents to be sued only by those with whom it has privity of contract." *Erickson Air Crane Co. of Wash. v. United States*, 731 F.2d 810, 813 (Fed.Cir.1984). Limited

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[3] The Court of Federal Claims suggested, *SoCal I*, 52 Fed.Cl. at 543, and the DMT Plaintiffs reiterate on appeal, that the government conceded that the Individual Plaintiffs are in privity of contract and therefore have standing to sue. Although the support for this assertion is weak, it is not necessary to address this argument because standing and privity of contract with the government are questions of subject matter jurisdiction that cannot be conceded to by a party. *Chancellor Manor v. United States*, 331 F.3d 891, 899 (Fed.Cir.2003).

exceptions to that general rule have been recognized when a party standing outside of privity stands in the shoes of a party within privity. *First Hartford Corp. Pension Plan & Trust v. United States*, 194 F.3d 1279, 1289 (Fed.Cir. 1999). Here, the Court of Federal Claims applied an expansive reading to the terms of the agreements at issue to conclude that the Individual Plaintiffs had standing to recover their claimed dilution damages. First, the Court of Federal Claims found that the Assistance Agreement, the RCMA and the FHLBB implementing resolutions should properly be considered components of one overall contract to which the Individual Plaintiffs were a party. *SoCal I*, 52 Fed.Cl. at 542. Accordingly, the court treated the government's promises regarding the treatment of supervisory goodwill and capital credits as running to all parties to the overall contract and determined that the Individual Plaintiffs had standing to recover. *Id.* In finding one overall contract, the court relied primarily on its interpretation of two clauses of the Assistance Agreement: the "Sole Benefit" clause and the "Entire Agreement" clause.

The Sole Benefit clause of the Assistance Agreement reads:

> It is the intention of the parties that this Agreement, the assumption of obligations and statements of responsibilities under it, and all of its conditions and provisions are for the sole benefit of the parties hereto and for the benefit of no other person. Nothing expressed or referred to in this Agreement is intended or shall be construed to give any person other than the parties hereto any legal or equitable right, remedy, or claim under, or in respect to, this Agreement or any of its provisions.

The government argued that the effect of the Sole Benefit clause was to limit the benefits of the Assistance Agreement to the Institutional Plaintiffs as parties to the contract. The Court of Federal Claims rejected this argument on the grounds that reading the Sole Benefit clause in that man-

ner would effectively nullify the Entire Agreement clause. *SoCal I*, 52 Fed.Cl. at 541.

The Entire Agreement clause of the Assistance Agreement reads in pertinent part:

> This Agreement, together with any interpretation or understanding agreed to in writing by the parties, constitutes the entire agreement between the parties and supersedes all prior agreements and understandings of the parties in connection with it, excepting only any resolutions or letters concerning the Conversion, the Acquisition or this Agreement issued by [FHLBB] or [FSLIC] in connection with the approval of the Conversion, the Acquisition and this Agreement.

On its face, the Entire Agreement clause specifically incorporates the Forbearance Letter from the FHLBB and the government does not contest that the letter should be considered part of the Assistance Agreement. *SoCal I*, 52 Fed.Cl. at 535. The Court of Federal Claims interpreted the Entire Agreement clause to also incorporate the RCMA. *Id.* at 541. Accordingly, the court determined that there was a direct conflict between the expansive terms of the Entire Agreement clause and the limitations of the Sole Benefit clause. *Id.* at 541. In order to avoid reading out of the contract the Entire Agreement clause, the court determined that the Sole Benefit clause was unenforceable. *Id.* at 542.

The Court of Federal Claims' reading of the Entire Agreement clause violates one of the basic precepts of contract interpretation—it does not comport with the plain meaning of the clause. *C. Sanchez and Son, Inc. v. United States*, 6 F.3d 1539, 1543 (Fed.Cir.1993) ("A contract is read in accordance with its express terms and the plain meaning thereof."); *see also Lowber v. Bangs*, 69 U.S. (2 Wall.) 728, 736 (1865) ("The construction to be put upon contracts of this sort depends upon the intentions of the parties, to be gathered

from the language of the individual instrument." (citation omitted)); *Foley Co. v. United States*, 11 F.3d 1032, 1034 (Fed.Cir.1993) ("Contract interpretation begins with the plain language of the agreement."). The Entire Agreement clause specifically incorporates only a) interpretations or understandings agreed to in writing by the parties; and b) resolutions or letters from the FHLBB or the FSLIC. The RCMA does not constitute either of the types of documents integrated into the Assistance Agreement. It is a separate contract that involves additional parties and distinct promises, including its own Entire Agreement clause. The RCMA does not purport to either interpret the Assistance Agreement or embody an understanding of the Assistance Agreement and there is no question that the RCMA is not a resolution or letter from the government regulators.

Not only does the Entire Agreement clause not reference the RCMA, the definition section of the Assistance Agreement identifies the RCMA as a separate agreement to be executed in substantially the form provided for in Exhibit A to the Assistance Agreement. Although the existence of the RCMA is acknowledged by the Assistance Agreement, the RCMA itself is neither explicitly incorporated into the Assistance Agreement nor implicitly incorporated by the Entire Agreement clause. *McAbee Constr., Inc. v. United States*, 97 F.3d 1431, 1434 (1996) (stating that the parties may expressly incorporate documentary or other evidence into a contract via an integration clause); *see also Winstar*, 518 U.S. at 861-68 (giving effect to contract integration clauses incorporating specific extrinsic documents as part of the contract). Furthermore, far from indicating that the Assistance Agreement and the RCMA should be read as constituting one contract, the plain language of the Sole Benefit clause and the Entire Agreement clause evidences the parties' intent to limit the scope of the Assistance Agreement to its specified terms. *Barron Bancshares, Inc. v. United States*, 366 F.3d 1360, 1375 (Fed.Cir.2004) (holding that an

integration clause conclusively establishes that the integration is total and prohibits the use of external evidence to add to or modify the terms of a written agreement).

In support of the Court of Federal Claims' expansive interpretation of the scope of the Assistance Agreement, the DMT Plaintiffs cite to a number of cases that purportedly establish that it is proper to read related instruments as constituting one single contract. The non-binding case law to which the DMT Plaintiffs cite does not stand for the proposition claimed, namely that a party to one contract can be deemed a party to a related contract simply because the separate contracts constitute components of one transaction. To the contrary, the cases cited apply a basic rule of contract interpretation to the effect that "where several instruments, executed contemporaneously or at different times, pertain to the same transaction, they will be read together, even though they do not expressly refer to each other." *Kurz v. United States*, 156 F.Supp. 99, 104 (S.D.N.Y.1957); *see also Peterson v. Miller Rubber Co. of New York*, 24 F.2d 59, 62 (8th Cir.1928); *Cf. Hampton Roads Shipping Assoc. v. Int'l Longshoremen's Assoc.*, 597 F.Supp. 709, 716 (E.D.Va.1984) (suggesting that several writings "will constitute a single contract as long as they involve the same subject matter and prove to be parts of an entire transaction;" despite the language used, the analysis undertaken by the court focused only on the meaning of a term used in multiple agreements). The issue before the Court of Federal Claims was not the construction of a common term, however, but rather the existence of an agreement between the government and the Individual Plaintiffs. The cases cited by the DMT Plaintiffs are not persuasive authority for ignoring the terms of the Assistance Agreement and extending the benefits of the contract to the Individual Plaintiffs who were not party to that contract.

The Court of Federal Claims premised its finding that the Individual Plaintiffs have standing to sue on its determination

that there was one overall contract to which the Individual Plaintiffs were "not ancillary, as the Government urges, but rather central to this transaction. The thrift would have failed—and the acquisition never have occurred—but for the Individual Plaintiffs." *SoCal I*, 52 Fed.Cl. at 542.[4] In so finding, the court focused on evidence suggesting that the Individual Plaintiffs initiated the conversion and acquisition processes prior to incorporating SCH and that at least some of them negotiated directly with the government in arranging the transaction. *Id.* at 533. Furthermore, the evidence showed that the government was aware both that the Individual Plaintiffs would be supplying the money used to rehabilitate SoCal and that the Individual Plaintiffs would be the primary shareholders of SCH. Contrary to the conclusion of the Court of Federal Claims, however, these roles of negotiator and shareholder do not bring the Individual Plaintiffs into privity of contract with the government in regards to the Assistance Agreement entered into with SCH and SoCal.

The court's emphasis on the Individual Plaintiff[s'] involvement in the conversion and acquisition processes fails to acknowledge that a corporation is generally considered to be a separate legal entity from its shareholder—a concept well grounded in state law. *Wenban Estate, Inc. v. Hewlett*, 193 Cal. 675, 227 P. 723, 731 (1924). Here, it is the law of California that governs the construction of the Assistance Agreement as specifically provided for in the "Governing Law" clause. Under California law, the corporate entity may be disregarded in order to prevent fraud, to protect third persons or to prevent a grave injustice, including an injustice to shareholders. *Cooperman v. Unemployment Insur. Appeals*

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[4] It is noteworthy that the Court of Federal Claims did not find that the status of the Individual Plaintiffs as signatories to the RCMA was sufficient to allow them to recover damages. The terms of the RCMA, and their inability to support the Individual Plaintiffs' claims for damages, are addressed in the following subsection.

Bd., 49 Cal.App.3d 1, 122 Cal.Rptr. 127, 131 (1975). In order for the acts and obligations of a corporation to be legally recognized as those of a particular person,

> the following combination of circumstances must be made to appear: First, that the corporation is not only influenced and governed by that person, but that there is such a unity of interest and ownership that the individuality, or separateness, of the said person and corporation has ceased; second, that the facts are such that an adherence to the fiction of the separate existence of the corporation would, under the particular circumstances, sanction a fraud or promote injustice.

Minifie v. Rowley, 187 Cal. 481, 202 P. 673, 676 (1921). Here, there is no allegation that the Individual Plaintiffs had the necessary unity of interest with SCH and its subsidiary SoCal or that continued recognition of the corporate form would work a grave injustice. Accordingly, there is no justification for the Court of Federal Claims' disregard of the corporate structure invoked by the Individual Plaintiffs in facilitating the acquisition and conversion of Old Southern. *See Aladdin Oil Corp. v. Perluss*, 230 Cal.App.2d 603, 41 Cal.Rptr. 239, 245 (1964) ("Parties who determine to avail themselves of the right to do business by means of the establishment of a corporate entity must assume the burdens thereof as well as the privileges. The alter ego doctrine is applied to avoid inequitable results not to eliminate the consequences of corporate operations.")

This court has regularly acknowledged the legal distinction between a corporation and its shareholders and rejected claims by shareholders to assert a breach of contract claim on behalf of the corporation. *First Hartford Corp.*, 194 F.3d at 1289 (holding that a shareholder lacks privity of contract to sue the government for *Winstar* damages when only the corporation entered into an agreement with the FDIC); *FDIC v. United States* ("*Karnes*"), 342 F.3d 1313, 1318 (Fed.

Cir.2003) (same); *Castle*, 301 F.3d at 1339 (dismissing shareholders' claims on the grounds that they had not established that the government had entered into a contract with them as individuals independent of their status as shareholders); *Cain v. United States*, 350 F.3d 1309, 1317 (Fed.Cir.2003) (stating that the holding that there was no contract between the government and the shareholders of a thrift was consistent with this court's prior cases addressing the issue). We have done so, in part, out of the recognition that "one of the principal motivations behind utilizing the corporate form is often the desire to limit the risk of ownership to the amount of capital invested and thus avoid the obligations, contractual or otherwise, of the corporation." *First Hartford*, 194 F.3d at 1289. Having chosen to limit their personal liability by adopting a corporate form, we have refused to allow shareholders to rely on their involvement in the negotiation process or their role in funding a transaction to alter their chosen legal status. *See Karnes*, 342 F.3d at 1319 ("Neither [the government's] knowledge, the supplying of the new capital, or the Lee's position as stockholders in Kames, made them parties to those arrangements."); *Cain*, 350 F.3d at 1315-17 (holding that the government's communication and negotiation with shareholders did not establish that the shareholders were parties to the contracts entered into between the government and the corporation). We reached a different result in *La Van v. United States*, 382 F.3d 1340, 1349 (Fed.Cir.2004), by focusing on factual distinctions between *Karnes* and *Cain* and the case presented in *La Van*. Specifically, we held that the shareholders were so critical to the conversion transaction that they, rather than the corporation, were essentially the direct purchasers of the converted federally-insured institution. *Id.* In *La Van*, however, unlike here, there was no indication that the parties identified state law intended to govern the contract. The factual analysis of *La Van* does not address the legal requirements imposed here, namely the strictures of California

law mandating a distinction between a corporation and its shareholders.

Not only do the Individual Plaintiffs not have standing in this case based on their status as shareholders, but we must also be mindful of the possibility that allowing such a suit would create an impermissible double recovery. The purpose of damages for breach of contract is generally to put the wronged party in as good a position as he would have been had the contract been fully performed. *See* Cal.Civ.Code § 3300 (2005); *Restatement (Second) of Contracts* § 347 cmt. a (1981). In light of this general purpose, a wronged party is typically not allowed to recover twice for the same harm, here a breach of contract. *See EEOC v. Waffle House, Inc.*, 534 U.S. 279, 297 (2002) ("[I]t goes without saying that the courts can and should preclude double recovery by an individual.") (internal citations omitted); *see also Chou v. Univ. of Chicago*, 254 F.3d 1347, 1365 (Fed.Cir.2001). This limitation applies even where claims exist under both contract and tort, *see, e.g., Ostano Commerzanstalt v. Telewide Sys., Inc.*, 880 F.2d 642, 649 (2d Cir.1989), or where a claim exists under a statutory provision and under common law, *see, e.g., Waffle House*, 534 U.S. at 297. California, by statute, limits damages in contract cases to those that a party "could have gained by the full performance thereof on both sides," unless additional damages are provided for by statute. *Cal.Code* § 3358 (2005). Since the compensation awarded the corporation flows to its shareholders through the value of their stock, to allow individuals to recover both through the corporation and as individuals would be to allow duplicative recovery. *See Gaff v. FDIC*, 814 F.2d 311, 315 (6th Cir.1987) ("a diminution in the value of corporate stock resulting from some depletion of or injury to corporate assets is a direct injury only to the corporation; it is merely an indirect or incidental injury to an individual shareholder"); *see also Vinci v. Waste Mgmt. of Alameda County, Inc.*, 80 F.3d 1372, 1375 (9th Cir.1996) (holding that a shareholder of

a corporation cannot recover directly for antitrust violations, because such would amount to double recovery.); *Stein v. United Artists Corp.*, 691 F.2d 885, 895-96 (9th Cir.1982) (prohibiting creditors and guarantors of a corporation from recovering separately on antitrust claims, because double recovery would result); *Hometown Fin., Inc. v. United States*, 56 Fed.Cl. 477, 486-87 (2003) (explaining that a shareholder suit against the government for breach of contract with a failed thrift presented serious risk of impermissible double recovery). The Individual Plaintiffs are not parties to the Assistance Agreement and therefore they do not have standing to sue the government for a breach of the promises made in that agreement.

B. The Ability of the Individual Plaintiffs to Recover Under the RCMA

Although the Individual Plaintiffs were not party to the Assistance Agreement, they were in contractual privity with the government under the RCMA. The question becomes, then, whether they are entitled to the damages they seek based on the terms of that contract.

There are four components of the RCMA relevant to this determination. First, Recital A indicates that "the [Individual Plaintiffs] collectively own 97.5 percent of the outstanding voting securities of [SCH] and control [SCH]." Second, Recital G and § 1 include the government's promise that SCH and SoCal will be able to account for $217.5 million in capital credits as part of its regulatory capital. Third, the RCMA states that "so long as [SCH] shall be obligated pursuant to § 1, the [Individual Plaintiffs], severally in proportion to their initial ownership of the common stock of [SCH] as reflected in the percentages set forth opposite their signatures below, hereby guarantee the performance of [SCH] and [SoCal] under § 1." Finally, the RCMA requires that the Individual Plaintiffs, or their successors who have assumed their shares of the guarantee and have not been objected to by

the FSLIC, shall "collectively own not less than a majority of the outstanding voting power of [SCH]."

The DMT Plaintiffs argue that the incorporation of the capital credit promise into the terms of the RCMA is sufficient to uphold the Court of Federal Claims' award of damages. This argument fails to recognize, however, that the damages for which the Individual Plaintiffs seek to recover, namely the dilution and extinguishment of their ownership interests in SCH, were not caused by the obligations they incurred in the RCMA. The RCMA did not require that the Individual Plaintiffs invest in SCH. To the contrary, Recital A indicates that the incorporation, ownership and control of SCH were established prior to the parties entering into the RCMA. At the most, the RCMA obligated the Individual Plaintiffs to collectively contribute to SCH and SoCal an additional $5 million in the event that SCH and SoCal did not maintain SoCal's regulatory capital at the required level. There is no indication that the government ever enforced this guarantee or that the Individual Plaintiffs ever complied with its terms.

Under the terms of the agreement, even if we assume that the passage of FIRREA constituted a breach of the RCMA, the Individual Plaintiffs are not entitled to recover the damages they seek under any applicable theory of contract damages. There are three forms of damages typically awarded to compensate for breach of a contract: expectation damages, restitutionary damages, and reliance damages. *Hansen Bancorp, Inc. v. United States*, 367 F.3d 1297, 1308 (Fed.Cir. 2004). Expectation damages give the non-breaching party the benefit of his bargain by putting him in as good a position as he would have been in had the contract been performed. *Bluebonnet Savings Bank, F.S.B. v. United States*, 266 F.3d 1348, 1355 (Fed.Cir.2001). "Expectation damages are recoverable provided they are actually foreseen or reasonably foreseeable, are caused by the breach of the promisor, and are

proved with reasonable certainty." *Id.* Restitutionary damages restore the non-breaching party to the position he would have been in had there never been a contract to breach. *Landmark Land Co., Inc. v. United States*, 256 F.3d 1365, 1372 (Fed.Cir.2001). Such damages, however, are not recoverable for actions taken voluntarily, beyond the obligations of the contract. *Id.* at 1375 ("the law is well settled . . . that in order to be compensable as restitution, the plaintiff's contribution must have been made in performance of its contractual obligations"). Reliance damages are damages designed to compensate a plaintiff for foreseeable loss caused by reliance on the contract. *Id.* at 1369. The Individual Plaintiffs are not entitled to recover dilution damages under any of these theories of recovery.

As a preliminary matter, it is worth noting that there are no terms in the RCMA that require the Individual Plaintiffs to raise capital for SCH and SoCal by diluting their ownership interest in order to issue equity to new investors. At the most, the RCMA obligates the Individual Plaintiffs to contribute an additional $5 million to the operation of SCH and SoCal. Accordingly, based on the unambiguous terms of the RCMA, the Individual Plaintiffs' loss of their ownership interests was neither the foreseeable result of nor caused by the government's breach of the RCMA and therefore dilution damages cannot be awarded as a form of expectation damages. Similarly, because the Individual Plaintiffs were not required to dilute their ownership interests, but voluntarily chose to do so, they cannot recover restitution for their actions. Furthermore, because the recapitalizations did not occur until after FIRREA was passed, it is axiomatic that the dilution of the Individual Plaintiffs' ownership interest was not undertaken in reliance on the government's promises regarding accounting for capital credits and supervisory goodwill. Accordingly, they do not have grounds to recover reliance damages. Finally, because the initial investment in SCH occurred prior to the execution of the RCMA, the

Individual Plaintiffs cannot point to that undertaking as grounds to recover under any of the applicable theories.

The Individual Plaintiffs do not have standing to sue under the Assistance Agreement and they cannot recover the damages they seek under the RCMA. The decision of the Court of Federal Claims holding the government liable to the Individual Plaintiffs and awarding damages to these parties is vacated. In light of this holding, it is not necessary to address the government's challenge to the amount of damages awarded to the Individual Plaintiffs or the DMT Plaintiffs' cross-claim for additional damages.

C. The Award to the Institutional Plaintiffs of the Replacement Cost of Capital

The Court of Federal Claims awarded the Institutional Plaintiffs $29,436,229.44 as compensation for the costs the Institutional Plaintiffs incurred in replacing the goodwill phased out by FIRREA.[5] *SoCal II*, 57 Fed.Cl. at 631. In association with the 1992 recapitalization, the court awarded the Institutional Plaintiffs $5,218,000 in transaction costs and expenses and $556,000 for the payment of dividends required by the issuance of the senior preferred stock in 1992. *Id.* In association with the 1995 recapitalization, the court awarded $714,374.04 in transaction costs and expenses, $3,508,000 in interest costs mandated by the recapitalization, and $19,439,855.40 for the payment of the accumulated dividends on all outstanding preferred stock issued in 1995. *Id.* The government does not challenge the $5,932,374.04 awarded for transaction costs and expenses, but contests the remainder of this award.

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[5] The court classified the awards to the Institutional Plaintiffs as a form of reliance damages, but they are more accurately considered a measure of expectation damages, designed to give the Institutional Plaintiffs the benefit of their bargain. *LaSalle Talman Bank, F.S.B. v. United States*, 317 F.3d 1363, 1374 (Fed.Cir.2003).

The government challenges the Court of Federal Claims' award of replacement costs of capital on two grounds. First, it argues that the holding of *California Federal Bank, FSB v. United States*, 245 F.3d 1342 (Fed.Cir.2001) limits any award for the replacement of goodwill to the transaction costs incurred in raising the replacement capital. Second, it finds error in the court's failure to account for any earnings that flowed to SoCal and SCH by having cash on-hand rather than nontransferable, amortizing goodwill.

The government reads *California Federal* to limit any award for replacing goodwill with real capital to the transaction costs incurred. *Cal. Fed.*, 245 F.3d at 1350. This interpretation of *California Federal* unreasonably expands the scope of the issue decided in that case. The court in *California Federal* did not hold that all awards for the replacement costs of capital should be limited to transaction costs, but simply that the Court of Federal Claims had not erred in rejecting the testimony of California Federal's expert, which would have established California Federal's right to damages in excess of its transaction costs. *Id.* The expert testimony that the court had found incredible was a claim that it cost the thrift nearly a billion dollars to replace $390 million of goodwill. *Id.* The decision in *California Federal* to limit the award of replacement costs of capital to the transaction costs incurred does not mandate a similar result in this case where the Institutional Plaintiffs presented very different, carefully itemized evidence in support of their claim.

The government's second challenge to the Court of Federal Claims' award of damages has more merit. As this court held in *LaSalle Talman Bank, F.S.B. v. United States*, 317 F.3d 1363, 1376 (Fed.Cir.2003), "payment of a return on capital reflects the cost of capital. However, in determining damages the benefits of that capital must be credited, as mitigation due to the replacement of goodwill with cash." In the case at hand, the Institutional Plaintiffs' expert acknowledged that his damage calculation was a complete accounting of all costs

that could be definitively measured, but that it did not include an offset for the income generated by the replacement capital because that income was not precisely measurable. In crafting its damages award, the Court of Federal Claims granted the Institutional Plaintiffs the entire amount established by their expert, which means that the award does not reflect the benefit of the capital that the Institutional Plaintiffs received. *SoCal II*, 57 Fed.Cl. at 631.

The government suggests that it was grave error for the Court of Federal Claims to fail to offset the damages award by the amount of benefit the Institutional Plaintiffs received from owning cash rather than goodwill. The true gravity of the error is unclear from the record established, however, and it is not possible to ascertain whether the Institutional Plaintiffs adduced sufficient evidence from which the court could "make a fair and reasonable approximation of the damages" properly accounting for the benefits obtained. *See Bluebonnet*, 266 F.3d at 1357. Accordingly, this issue is reversed and remanded to the Court of Federal Claims for further fact-finding in order to determine if a complete determination of damages can be reached.

D. The Award to the Institutional Plaintiffs for Wounded Bank Damages

The Court of Federal Claims awarded the Institutional Plaintiffs $35,961,591.97 in damages for wounded bank expenses, i.e. increases in its costs due to being identified as a "troubled" institution. *SoCal II*, 57 Fed.Cl. at 628. The court calculated the amount of wounded bank damages as follows: $32,320,000 for excess cost of funds; $278,258.55 for legal, consulting and filing fees; $64,879.42 for FHLBB Collateral delivery fees; $2,509,000 for FDIC deposit insurance premiums; and $789,454 in excess assessments paid to the government's Office of Thrift Supervision. *Id.* The government challenges the court's award of wounded bank damages on the grounds that: (i) as a matter of law, the damages are

too remote from the breach to be recoverable; (ii) the finding that the damages were caused by the breach was clearly erroneous; and (iii) the measurement of excess costs of funds was based on flawed expert testimony.

The government's first challenge to the Institutional Plaintiffs' claim for wounded bank damages is that it is too remote as a matter of law. The government argues that in order to reach the claimed wounded bank damages an extended chain of causation must be followed that indicates that the Institutional Plaintiffs are seeking consequential damages beyond those typically permitted in contract actions. *See Wells Fargo Bank, N.A. v. United States*, 88 F.3d 1012, 1021-23 (Fed. Cir.1996). This argument raises the question whether the increased costs of funds were reasonably foreseeable at the time the contract was entered into. Contrary to the government's characterization, foreseeability is a question of fact reviewed for clear error. *Bluebonnet*, 266 F.3d at 1355. The government does not, however, address why it would be unforeseeable that the loss of the contracted-for benefits would impact the health of SoCal and increase its costs of doing business, particularly since the regulatory treatment at issue was designed to foster the recovery of ailing thrifts. The government also fails to acknowledge this court's approval of similar damage theories in *Winstar*-related cases. *See Bluebonnet*, 266 F.3d at 1355-56 (approving a thrift's claim to recover the increase in financing costs caused by the passage of FIRREA); *Glendale Fed. Bank, FSB v. United States*, 378 F.3d 1308, 1311-12 (Fed.Cir.2004) (affirming the trial court's award of wounded bank damages to compensate a thrift for the higher costs of conducting its general business after FIRREA). The government's argument that wounded bank damages are not recoverable as a matter of law is without merit.

The government's second challenge to the award of wounded bank damages is an attack on the Court of Federal Claims' determination that the damages were caused by

FIRREA. "Causation is . . . a question of fact reviewed under the clear error standard." *Bluebonnet*, 266 F.3d at 1356. The Court of Federal Claims concluded that FIRREA was the principal cause of SoCal's recapitalization and was the substantial factor in SoCal's incurring higher costs of funds after the breach. *SoCal II*, 57 Fed.Cl. at 616. In so holding, the court considered and discounted evidence regarding the impact on SoCal's operations of the recession in California, the massive decline in real estate values, losses stemming from the Los Angeles riots following the Rodney King trial and the Northridge earthquake. *Id.* The government does not attack this fact finding directly, but attempts to undermine the factual conclusions on which it was based. The government asserts that the breach did not cause SoCal to fall out of capital compliance, did not cause negative publicity for SoCal, did not disrupt SoCal's planned branch expansion, did not cause SoCal's interest rate risk and hedging problems, and did not cause an increase in SoCal's funding costs. Although there is certainly merit to the government's claim that SoCal was a relatively weak institution prior to the passage of FIRREA, the government is not persuasive in arguing that because of that weakness FIRREA had no effect on the thrift's operations. There is certainly evidence to support the government's claims, but there is also countervailing evidence consistent with the court's conclusions. At its base, the government's causation argument is nothing more than a request that this court reweigh the evidence heard by the Court of Federal Claims and come to a different conclusion. The government has not established that it was clear error for the court to conclude that the passage of FIRREA lead to specific and quantifiable increases in the thrift's cost of doing business.

Finally, the government challenges the evidentiary support for the court's award of wounded bank damages. Specifically, the government argues that the testimony of Dr. Hartzog, the Institutional Plaintiffs' expert on wounded bank

damages, was procedurally flawed and that it lacked credibility. The government also asserts that it was penalized by the court for not presenting an alternative damages model. Neither of the government's arguments have merit. The government presented its challenges to the credibility of Dr. Hartzog's testimony at trial and, despite those challenges, the Court of Federal Claims found Dr. Hartzog's testimony to be "entirely accurate and credible" and supported by other experts and witnesses. *SoCal II*, 57 Fed.Cl. at 630. The government's invitation to overturn the court's credibility determination is not well-founded. *Syntex LLC v. Apotex, Inc.*, 407 F.3d 1371, 1384 (Fed.Cir.2005) ("Credibility determinations are the type of factual determinations that are best left to the fact finder, the trial court."). Nor is there merit to the government's argument that it was penalized for failing to present an alternative damage theory, because the court simply indicated that the government's failure to present such a model undermined its efforts to challenge the model presented by the Institutional Plaintiffs. The Court of Federal Claims' award of wounded bank damages is affirmed.

III. CONCLUSION

For the foregoing reasons, we vacate both the determination of the Court of Federal Claims holding that the Individual Plaintiffs had standing to sue and the award of damages based on that suit. We reverse the court's award of replacement costs of capital and remand for further proceedings consistent with this opinion. Finally, we affirm the court's award of wounded bank damages.

AFFIRMED IN PART, REVERSED IN PART, VACATED AND REMANDED.

IV. COSTS

No costs.

MAYER, *Circuit Judge*, dissenting in part.

The combined content of the Regulatory Capital Maintenance Agreement ("RCMA"), the Assistance Agreement, and the Federal Home Loan Bank Board ("FHLBB") implementing resolutions, all signed on the same day, proves that the Individual Plaintiffs* entered into an overall contract with the government. The promises and obligations within these documents were intended to personally benefit and burden them, independent of their status as shareholders.

At the contract formation stage, the Individual Plaintiffs were the government's only counterparties for purposes of negotiation. Before the acquisition that gave rise to this case, Southern California Savings and Loan Association ("Old Southern") was insolvent and the Federal Savings and Loan Insurance Company ("FSLIC") bore full responsibility for its liabilities. To avoid liquidation, the government actively solicited prospective purchasers or merger partners who might rescue the troubled institution. *S. Cal. Fed. S & L Ass'n v. United States*, 52 Fed.Cl. 531, 533 (2002) ("*SoCal I*"). In response, the Individual Plaintiffs submitted a bid expressly conditioned upon the government's promise of substantial capital forbearances. *Id.* at 535. To this end, they alone negotiated with the government, and Southern California Federal Savings and Loan Association ("SoCal") was later created through the performance of the contract, via a supervisory conversion that occurred at the closing of the transaction on April 30, 1987.

The issue is whether the "government made any promises, contractual or otherwise, that were expressly intended to benefit the shareholders personally, independently of their status as shareholders." *Castle v. United States*, 301 F.3d 1328, 1338 (Fed.Cir.2002). The government contends that

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* The Individual Plaintiffs include: Arbur, Inc., the Estate of William E. Simon, Sr., Roy Doumani, Preston Martin, and Beverly W. Thrall.

the Individual Plaintiffs were mere investors in SoCal Holdings, Inc ("SCH"). This narrow characterization, however, ignores the personal and individual contractual obligations that they assumed pursuant to the RCMA. As the trial court found, "[t]he Government specifically required the Individual Plaintiffs to sign and execute the RCMA before [the government] would 'provide [the] financial assistance and indemnification[s] set forth in the Assistance Agreement.'" *S. Cal. Fed. S & L Ass'n v. United States*, 57 Fed.Cl. 598, 605 (2003) ("*SoCal II* ") (quoting RCMA, Recital "E," p. 2). Moreover, "[t]he personal guarantees represented by their individual signatures provided extra security to the Government that the Individual Plaintiffs would not walk away from the ailing thrift. [The RCMA] imposed obligations on the private signatories for up to 12 years." *Id.*

While this court is correct that the Entire Agreement clause contained in the Assistance Agreement does not expressly incorporate the RCMA, it fails to accord appropriate weight to the fact that "the very validity of the Assistance Agreement was conditioned upon the Individual Plaintiffs' execution of the RCMA: 'The [FSLIC]'s obligations pursuant to this Agreement are also conditioned upon the following: . . . The execution and delivery by [SCH], [SoCal], and the Investors [each Individual Plaintiff . . .], as appropriate, of the Regulatory Capital Maintenance Agreement. . . .'" *SoCal I*, 52 Fed.Cl. at 542 (quoting the Assistance Agreement, sec. 2(b)). The Individual Plaintiffs were essential to the formation of the overall contract in their individual capacities because the FHLBB "explicitly conditioned its approval of the transaction on the execution of the RCMA by the FSLIC, SCH, SoCal, and the Individual Plaintiffs." *Id.* (citing FHLBB Res. 87-511, p. 7). The RCMA is the basic contract document of the transaction on which all other agreements depend. *See Castle*, 301 F.3d at 1339 (referring to the RCMA at issue as the "main document comprising the alleged contract"). Accordingly, the combined documents constitute

an overall contract giving the Individual Plaintiffs standing to enforce both the capital credit and the supervisory goodwill promises of the government and I would affirm the Court of Federal Claims on this point.

APPENDIX B

UNITED STATES COURT OF FEDERAL CLAIMS

No. 93–52C

SOUTHERN CALIFORNIA FEDERAL SAVINGS & LOAN ASSOCIATION; SOCAL HOLDINGS, INC.; ARBUR, INC.; ROY DOUMANI; PRESTON MARTIN; WILLIAM E. SIMON, JR., J. PETER SIMON, GEORGE J. GILLESPIE, III, Executors of the Estate of William E. Simon, Sr.; and BEVERLY W. THRALL, Successor to the Claims of Larry B. Thrall,

Plaintiffs,

v.

THE UNITED STATES OF AMERICA,

Defendant.

Aug. 7, 2003
As corrected Sept. 24, 2003
Reconsideration denied Oct. 3, 2003

OPINION

BASKIR, *Judge*.

I. *Introduction*

This is a case against the United States by a California savings and loan association, its holding company, and the individuals who helped rescue the thrift's failing predecessor by forming and leading the new institution. In a previous opinion we held that the Plaintiffs had an express contract with the Defendant to treat as regulatory capital a $217.5 million capital credit provided by the Government in 1987 to the newly-formed Southern California Federal Savings and Loan Association and the $79.6 million in supervisory goodwill created as a result of SoCal's acquisition of Old

Southern (its failing predecessor), and to amortize those amounts over a 25-year period. *See S. Cal. Fed. Sav. & Loan Assoc. v. United States*, 52 Fed.Cl. 531 (2002) (*Liability Opinion*).

Following the guidance of the U.S. Court of Appeals for the Federal Circuit and the U.S. Supreme Court in *United States v. Winstar Corp.*, 518 U.S. 839 (1996) (*Winstar IV*), *aff'g*, 64 F.3d 1531 (Fed.Cir.1995) (*en banc*) (*Winstar III*), we further held that this contract was breached by the passage of the Financial Institutions Reform Recovery and Enforcement Act of 1989 (FIRREA), Pub.L. No. 101-73, 103 Stat. 183 and its implementing regulations, which eliminated SoCal's ability to count goodwill as regulatory capital.

The Plaintiffs seek a variety of damages resulting from this breach. Following an extended trial on damages, we award the Plaintiffs some of these claimed damages, and deny others. In summary, we award SoCal and its holding company, SoCal Holdings, Inc., $65,397,821.41 in "wounded bank" and "cost of replacement capital" damages.

We award $12,891,113.75 in "dilution" damages to the "Simon Plaintiffs," Arbur, Inc. and William E. Simon, Jr., J. Peter Simon, and George J. Gillespie, III, the Executors of the Estate of William E. Simon, Sr. In addition, we award $6,223,280.00 in "dilution" damages to both Mr. Roy Doumani and Mrs. Beverly W. Thrall, the Executor of the Estate of Larry B. Thrall. Finally, we award Mr. Preston Martin $3,333,900.00, also in "dilution" damages.

II. *Background*

In our opinion resolving liability, we reviewed the history of the *Winstar* litigation and explained the case management process set up by the Court of Federal Claims to resolve the approximately 120 cases filed in the wake of the *Winstar* decisions. In addition, we set forth in detail the transaction at issue in this case and the documents that formed the binding

contract on which the Plaintiffs now claim damages. Before setting forth the facts found at the trial on damages, a review of the procedural history and the parties to the instant case provides context to this Opinion.

A. Parties

In the mid-1980's, one-hundred-year-old Southern California Savings and Loan Association (Old Southern), based in Beverly Hills, California, a large institution with assets in the $1 billion range, was suffering "serious asset problems" from "large operating losses, weak management, poor quality control and underwriting standards, and large contingent liabilities." *Liability Opinion*, 52 Fed.Cl. at 533 (citations omitted).

On June 7, 1985, the Federal Home Loan Bank Board (FHLBB), pursuant to its statutory authority over Federally insured savings institutions, placed the insolvent thrift into receivership under the control of the Federal Savings and Loan Insurance Corporation (FSLIC). For the next year, as an alternative to liquidating the thrift and expending the FSLIC's limited insurance funds, the FHLBB and FSLIC solicited prospective purchasers or merger partners who might rescue the deeply troubled institution. *Id.*

In response to these solicitations, the late former U.S. Treasury Secretary William E. Simon, Sr. formed a group of investors including, among others, former Federal Reserve Vice–Chairman and former FHLBB Chairman Preston Martin, California real estate investors Roy Doumani and the late Larry B. Thrall, and Arbur, Inc., an investment company owned by Secretary Simon and his children. In late 1986, Secretary Simon's group submitted to the FSLIC a bid to acquire the thrift. The members of Secretary Simon's group are referred to collectively as the "Individual Plaintiffs."

The Individual Plaintiffs proposed to form and capitalize personally a holding company, to be named SoCal Holdings,

Inc. (SCH), which would in turn purchase the failing thrift and form a new savings and loan association. Upon Government approval, the new association, named Southern California Federal Savings and Loan Association (SoCal), would acquire all of the assets and liabilities of its predecessor. The group's proposal contained a business plan which it believed would return SoCal to solvency and, eventually, profitability. Together, SoCal and its holding company are referred to as the "Institutional Plaintiffs" or the "SoCal Plaintiffs."

B. Procedural Background

The Plaintiffs initiated this lawsuit in 1993. Two years later, on August 2, 1995, the Plaintiffs filed a first amended complaint alleging that, by enacting FIRREA in 1989, the Government breached an express contract (Count 1), an implied-in-fact contract (Count 2), and the duty of good faith (Count 3). The Plaintiffs also seek restitution for breach of the alleged contract (Count 4), and further allege that the Government committed a taking without just compensation (Count 5) and violated the Plaintiffs' due process rights (Count 6). The Complaint and the Amended Complaint, and supporting documents, were originally filed under seal. We unsealed those and other documents, and lifted the *Winstar*-related Amended Master Protective Order from its application to this case last year. *See S. Cal. Fed. Sav. & Loan Assoc. v. United States*, 52 Fed.Cl. 20 (2002).

Since 1995 some of the parties' names have changed. On July 1, 1997, SoCal changed its name to People's Bank of California and SoCal Holdings, Inc. to PBOC Holdings, Inc. Four years later, on November 13, 2001, People's Bank of California merged with California National Bank, with California National Bank the surviving institution. California National Bank is the successor-in-interest to SoCal and, together with PBOC Holdings, Inc., continues to pursue the thrift's claim on behalf of the named plaintiffs, Southern

California Federal Savings and Loan Association and SoCal Holdings, Inc. For ease of reference, the parties and the Court continue to refer to the Institutional Plaintiffs as SoCal and SCH.

Upon Mr. Thrall's death in 1998, Beverly W. Thrall, Mr. Thrall's wife, was substituted as a Plaintiff, pursuant to Court of Federal Claims Rule 25(a). Upon Secretary Simon's death in 2000, William E. Simon, Jr., J. Peter Simon, and George Gillespie, III, the Executors of the Estate of William E. Simon, Sr., were substituted as Plaintiffs, also pursuant to Rule 25(a). Because Mr. Doumani, Mr. Martin, and Mrs. Thrall eventually obtained their own counsel and submitted individual pleadings on their behalf, we refer to this group as the "DMT Plaintiffs." Likewise, Arbur, Inc. and the Executors of Secretary Simon's estate are referred to as the "Simon Plaintiffs."

Several participants to the 1987 transaction are not present in this case. The Ariadne Group, an original investor in SoCal, filed its own independent complaint on these same facts. Its case was dismissed as untimely under the governing statute of limitations. *See Plaintiffs in Winstar-Related Cases v. United States*, 37 Fed.Cl. 174, 182–84 (1997), *aff'd. Ariadne Fin. Serv. Pty. v. United States*, 133 F.3d 874 (Fed.Cir.1998). Its motion to intervene in this case was also denied. *See S. Cal. Fed. Sav. & Loan Assoc. v. United States*, 51 Fed.Cl. 114 (2001). FIMA, another original SoCal shareholder, apparently did not join in this complaint or file its own.

In addition, two members of Secretary Simon's original group did not join in either the 1993 complaint or the 1995 amended complaint. Mr. Craig Godsen, an investor and party to the 1987 contract, has never sought to be a party to this lawsuit. Another contract signatory, former assistant Treasury Secretary Gerald Parsky, filed his own independent lawsuit related to the SoCal transaction. Mr. Parsky's

complaint was also dismissed on statute of limitations grounds, as was his motion to intervene. *See S. Cal. Fed. Sav. & Loan Assoc. v. United States*, 51 Fed.Cl. 676 (2002) (denying reconsideration); *see also* 52 Fed.Cl. 444 (2002) (denying intervention).

On May 10, 2002, the Court issued its fifth published opinion in this litigation and addressed Count 1 of the Plaintiffs' Amended Complaint. *See Liability Opinion*, 52 Fed.Cl. at 531. In that opinion, we found that both the Institutional Plaintiffs and the Individual Plaintiffs were parties to an express contract with the Government that it breached upon the enactment of FIRREA and its implementing regulations. In dismissing each of the Defendant's defenses, we noted that at least six Justices on the Supreme Court, and numerous Federal Circuit and Claims Court judges had rejected these defenses repeatedly. *See Id.* at 544–48.

Trial was held in this case for two months in the summer of 2002. Thereafter, the parties engaged in lengthy post-trial briefing, and submitted extensive proposed findings of fact. Consequently, this Opinion is the product of over one hundred hours of detailed expert and fact witness testimony, thousands of exhibits, a five thousand page trial transcript, hundreds of pages of post-trial briefing, and excellent advocacy on the part of the twenty-some attorneys who participated in the trial.

III. *Findings of Fact*

A. Contract Formation

The facts we recite are taken from the Liability Opinion, as well as from trial testimony and exhibits.

The Individual Plaintiffs' bid proposal regarding Old Southern was conditioned upon the receipt of substantial direct financial assistance from the Government and certain regulatory forbearances regarding minimum capital require-

ments. Capital requirements are "minimum reserves"—computed as a percentage of total liabilities—that the Government requires a savings and loan to maintain. *Winstar III*, 64 F.3d at 1535. The failure to "comply with minimum regulatory capital requirements [has] severe repercussions for a thrift." *Id.*

As then-Chairman of the U.S. Securities and Exchange Commission Richard C. Breeden noted in 1991:

> Capital requirements are the most powerful source of discipline for financial institutions. When maintained at an appropriate level, capital requirements reduce the incentive to take excessive risks and provide a cushion against loss.

Richard C. Breeden, "Thumbs on the Scale: The Role That Accounting Practices Played in the Savings and Loan Crisis," 59 *Fordham L.Rev.* S71, S75 (1991), cited with approval in *Winstar IV*, 518 U.S. at 845–851.

The bid also specifically proposed that the newly formed institution would account for the transaction "under purchase accounting" and that:

> any excess of fair value of liabilities over the fair value of assets would be recorded as an intangible asset ("goodwill") which would be amortized over 25 years using the straight-line method, without adjustment for any reason.

Bid Proposal, at p. 8–9.

The purchase method of accounting is a generally accepted accounting practice (GAAP) for mergers. *See Winstar III*, 64 F.3d at 1535.

In January, 1987, the FSLIC accepted the Individual Plaintiffs' bid in principle and thereafter a series of exchanges took place to complete the deal. Although the dollar amount of the Government's direct cash contribution changed several times,

the essential form of the transaction—a supervisory conversion using the purchase method of accounting and the infusion of cash from both the Government and several private parties—remained constant.

This transaction was executed on April 30, 1987, and was embodied in a series of inter-related documents signed by various of the parties, including the FSLIC, FHLBB, SoCal, SCH, and the Individual Plaintiffs. These documents include:

> (1) Assistance Agreement (AA), signed by FSLIC, SoCal, SCH (JX 1427);
>
> (2) Regulatory Capital Maintenance Agreement (RCMA), signed by FSLIC, SoCal, SCH, and each Individual Plaintiff (JX 1428);
>
> (3) FHLBB Resolution No. 87-511, reciting the particulars of the transaction; approving the supervisory conversion from a mutual to a stock association; approving the use of the capital credit in meeting regulatory minimum requirements; and approving the use of the purchase method of accounting with a 25-year amortization period (JX 1425);
>
> (4) FHLBB Implementation Resolution No. 87-513, approving the FSLIC's expenditure of money to the new association (JX 1425); and
>
> (5) Forbearance Letter from FHLBB to SCH (dated May 27, 1987), approving the use of the purchase method of accounting and the use of the FSLIC cash contribution towards meeting the regulatory capital requirements (JX 1426).

The Assistance Agreement contained the following integration clause:

> This Agreement, together with any interpretation or understanding agreed to in writing by the parties,

> constitutes the entire agreement between the parties and supersedes all prior agreements and understandings of the parties in connection with it, excepting only any resolutions or letters concerning the Conversion, the Acquisition or this Agreement issued by the Bank Board or the [FSLIC] in connection with the approval of the Conversion, the Acquisition, and this Agreement.

Assistance Agreement, sec. 18(a).

There is no disagreement among the parties that the documents referred to in the integration clause included, at a minimum, the RCMA, as well as FHLBB Resolutions 87–511 and 87–513, and the FHLBB Forbearance Letter to SCH.

Together these documents recited the following cash components of this complex transaction. First, the Individual Plaintiffs arranged for the infusion of approximately $40 million in private funds into SoCal and SCH. Second, after the FSLIC converted SoCal from a mutual savings and loan association to a stock savings and loan association, the new holding company purchased all of SoCal's common stock. Third, the FSLIC made a direct cash contribution to SoCal in the amount of $217.5 million, known throughout the *Winstar* litigation as the FSLIC "capital credit."

The private funds originated from a variety of sources. Two investment companies, Alapim Holdings, B.V., a Netherlands corporation (whose successors-in-interest are Ariadne Financial Services Partnership, Ltd. and Memvale Partnership, Ltd., collectively referred to as the "Ariadne Group") and FIMA Finance Management, Inc. (FIMA), purchased 100,000 shares of SoCal preferred stock for $33.3 million and 100,000 shares of SCH preferred stock for $1.7 million. The Ariadne Group also loaned the individual members of Secretary Simon's group a total of $5.8 million. The Individual Plaintiffs then used most of those funds ($5.1 million) to capitalize the holding company. In return, the

Individual Plaintiffs received differing amounts of SCH common stock.

The corporate structure of SCH dictated that any profits of SoCal were to be split 60/40 in favor of the common stock holders. The Simon Plaintiffs and their attorney Gerald Parsky (who is not a party) both received the largest shares of the common stock, each holding 29.744% of the shares. Mr. Doumani and Mr. Thrall received 14.359%, while Mr. Preston received 7.692%. The other non-party investor, Mr. Gosden, received 4.103%. These percentages are important to note so that the Court can trace what happened to the Individual Plaintiffs' ownership interest throughout the period in dispute. They also form the basis for the award to the Individual Plaintiffs. It is also important to note that the Individual Plaintiffs were not just involved with SoCal; as a group, they participated in transactions with at least two other savings and loan associations. *See, e.g., Westfed Holdings, Inc. v. United States*, 55 Fed.Cl. 544 (2003).

The primary Government documents approving the merger, FHLBB Resolution 87–511 and the FHLBB Forbearance Letter, required SoCal to submit to the FSLIC professional opinion letters regarding the transaction. First, SCH and the Individual Plaintiffs, no later than thirty days after the close of the transaction, were required to submit an opinion of counsel letter stating, among other required items, that the AA and the RCMA "constitute valid and binding obligations" upon SoCal, SCH and the Individual Plaintiffs. Res. 87-511, paras. 12–13. Second, SoCal and SCH were required to submit an "analysis accompanied by a concurring opinion from independent public accountants" verifying that SoCal accounted for the transaction under GAAP, except where the FHLBB and the FSLIC granted SoCal exceptions from compliance with GAAP. Res. 87–511, p. 13; Forbearance Letter, para. 2. The parties all agree that these docu-

ments were submitted in accordance with the conditions set forth in the FHLBB Resolution and Forbearance Letter.

The transactional records also contained several crucial mutual promises running between various of the parties. First, the RCMA, which was signed by the FSLIC, SoCal, SCH, Arbur, in their corporate capacities, and Messrs. Doumani, Martin, Simon, and Thrall in their individual capacities, contained a personal guarantee from each of the Individual Plaintiffs to infuse up to an additional $5 million dollars into SoCal should its capital fall below a certain level. RCMA, sec. 4.

Second, the RCMA specifically stated that SoCal could credit the $217.5 million Government capital contribution towards its regulatory net worth account. RCMA, sec. 1; Res. 87-511, para. 21(b); Forbearance Letter, para. 2(a).

Third, as proposed, SoCal could account for the acquisition using the purchase method of accounting, which brings about the recognition of goodwill for accounting purposes. AA, sec. 13; Res. 87–511, para. 21(a); Forbearance Letter, para. 2(b). Because the FSLIC supervised all transactions at issue in these *Winstar* cases, this goodwill has become known as "supervisory goodwill." On April 30, 1987, SoCal booked approximately $79.6 million in supervisory goodwill.

Fourth, FHLBB approved SoCal's request that the supervisory goodwill could be amortized over twenty-five years using the straight line method. Res. 87-511, para. 21(c); Forbearance Letter, para. 2(b).

Fifth, the RCMA also contained a clause that if the regulatory capital fell below 3% of SoCal's assets, the FSLIC could repossess the institution. RCMA, sec. 7. This provision of the RCMA, along with the Individual Plaintiffs' personal cash guarantee, is key to understanding the deal. The Government specifically required the Individual Plaintiffs to sign and execute the RCMA before it would "provide

[the] financial assistance and indemnification[s] set forth in the Assistance Agreement." RCMA, Recital "E", p. 2. The experience and reputation of Secretary Simon's investment group was considered an important intangible asset in the *rejuvenation of the thrift. The personal guarantees repre*sented by their individual signatures provided extra security to the Government that the Individual Plaintiffs would not walk away from the ailing thrift. This document imposed obligations on the private signatories for up to 12 years.

Taken together, the intangible goodwill promise and the tangible capital credit represented almost $300 million of Government assistance, direct and indirect, in exchange for the Individual Plaintiffs' time, leadership, and money in rescuing the failing thrift. The cost to the Government to liquidate the thrift and close it down was approximately $235 million, by at least one estimate at that time. As the Government document approving the acquisition stated, the FSLIC's expenditure of over $200 million, the use of goodwill, and "the acquisition of SoCal by SoCal Holdings . . . lessen[ed] the risk to the FSLIC." Res. 87-511, Marketing and Acquisition Finding No. 6, p. 17.

The Court previously found that all of these documents together constitute a "Final Contract," integrating the whole transaction, and creating mutually supporting obligations between the Government and each of the Plaintiffs. *See Liability Opinion*, 52 Fed.Cl. at 549.

B. Note on MACRO/CAMEL Ratings

The FSLIC, and later the Office of Thrift Supervision (OTS) and the Federal Deposit Insurance Corporation (FDIC), conducted periodic, regular full-scope and special, occasional examinations of SoCal and SCH, as they did of other thrifts. These examinations included an assessment of the following areas: the effectiveness of the management and the Board of Directors, asset quality, capital adequacy,

asset/liability and risk management, and earnings (operations). Originally going by the anagram MACRO, the denomination changed to CAMEL (capital, assets, management, earnings, liability) after FIRREA. The examiner would then prepare an exam report and assign ratings for each individual category, and one overall composite rating. Despite its formal status as a composite or uniform financial institution rating, the testimony of the various regulators and experts made clear that a thrift's capital position was the heaviest weighted of the categories.

Under the composite rating definitions, institutions were rated on a numerical basis: institutions that are a(1) are sound in every respect and give no cause for supervisory concern; institutions that are a(2) are fundamentally sound, but may reflect modest weaknesses that are correctable in the normal course of business; institutions that are a(3) exhibit a combination of financial, operational, or compliance weaknesses ranging from moderately severe to unsatisfactory, although the possibility of failure is remote; institutions that are a(4) have an immoderate number of serious financial weaknesses or a combination of other conditions that are unsatisfactory, they are subject to operational limitations and special scrutiny; and institutions that are a(5) have an extremely high immediate or near-term probability of failure, and will require some form of emergency assistance, merger, or acquisition. *See* JX 1152 at ii (OTS Report of Examination, Feb. 9, 1995).

The parties regularly referred to SoCal's MACRO or CAMEL ratings at various points throughout the trial as a uniform system to describe the condition of the thrift at a given point in time, and we shall do the same.

C. Post–Contract Operations

As of February 1987, just two months before the contract was signed, Old Southern was operating with a net worth of

negative $160.7 million and was incurring additional losses averaging $500,000 per month. *See* DX 28 (Memorandum from Alvin W. Smuzynski of the Federal Home Loan Bank System to Jeff Sconyers re: Acquisition of Southern California S & LA by SoCal Holdings, Inc., Apr. 28, 1987). Thus, by the time of the Acquisition, Old Southern had a MACRO rating of 5.

Accordingly, as Mr. Martin testified regarding the regulatory goodwill of $79.6 million and the capital credit of $217.5 million, the "[t]he promise of that $300 million [in regulatory capital] was the number one factor in our acquiring this institution. Without that $300 million, we would have said to them, this is 100-year-old institution, it's a mutual, its management record up to date is inadequate, and no, we don't want to buy Southern California, thank you." Tr. at 443.

As we have noted, the Government's contractual regulatory capital promises provided a substantial capital cushion that gave added protection to the Plaintiffs' investment, and were central to the new ownership team's business plan. More capital permits a thrift to grow by adding more deposits and borrowings. These funds can then be invested in earning assets. *See Liability Opinion*, 52 Fed.Cl. at 548; PX 0340A-C (Charts Outlining "How Thrift's Make Money").

Shortly after the 1987 Acquisition, Mr. John M. Yunker, Jr., was hired as the president and chief operating officer of SoCal. Mr. Yunker immediately began hiring senior managers for the key positions at SoCal. Among the officers hired by Mr. Yunker was E. John Doyle as Senior Vice President for retail banking, who also testified at trial.

SoCal's new management faced significant challenges following the 1987 acquisition. The testimony and vast documentary evidence illustrate the depth and range of problems plaguing SoCal's lending operations, accounting

functions, public image, and branch system by the time the new board of directors and management team were in place. Further, SoCal was burdened with a great number of inherited problem assets and lawsuits. Mr. Yunker testified that Old Southern "had been operating as a troubled institution, it was well-known that they were a failed institution," and SoCal had to "get back into a marketing program and reestablish our reputation as a viable, profitable institution, not as a failed institution. We were carrying a lot of baggage." Tr. 804-805.

SoCal's approved Business Plan focused on providing economical home financing and other financial products to its customers and a safe place to deposit their funds. *See* PX 0232 (SCH 5-Year Business Plan). The approved Business Plan projected growth in SoCal's assets from approximately $1 billion to $3.7 billion between 1987 and 1992.

Mr. Eric D. Shand, a FHLBB (and later OTS) supervisory agent and Western Regional Director, testified at trial and recalled SoCal's plan to grow significantly while maintaining compliance with its regulatory capital requirements. *See* Tr. 4106. Mr. Shand acknowledged that the FHLBB was fully aware of SoCal's plan to grow to over $3.5 billion in asset size. *See* Tr. 4110.

Because SoCal was a "start-up operation," its approved Business Plan did not project net income until 1990. *See* PX 0232 (Business Plan). The Government's supervisory agents concurred that, at this time, SoCal was "essentially a start-up operation." *See, e.g.*, DX 66 at 2 (Memorandum from OTS Supervisory Agent Sidney Mar to Messrs. Shand, Chin, Lee and McManus re: Southern California FS & LA, Jan. 12, 1988); Tr. 3585(Mar); Tr. 4041, 4113-4114 (Shand).

This start-up operation had to rebuild its branch system. As Mr. Doyle said, the "physical facilities were in poor shape and had not been refurbished in years, the carpets were threadbare, and the branches needed painting." Tr. 583.

SoCal had to dispose of or reduce its problem assets, write off its failed loans, and settle the numerous lawsuits against it. New management's task was also to improve operating efficiency, reduce its funding costs, and revise its investment and risk management policies.

It also badly needed to attract new deposits. SoCal President Yunker testified that the core deposits had materially weakened and had runoff significantly during the period of Old Southern's receivership. *See* Tr. 805.

The new management team was very successful during the period 1987-1989 in resolving many of these problems. In a July 1989 memo to the SCH Board of Directors, Mr. Yunker noted that by that date, among other things, all of the key management had been hired, policies and internal controls were in place in all major operating areas, core operations continued to improve, major problem assets had been substantially resolved, more than 100 lawsuits had been settled or terminated, branch deposits had been expanded significantly, the loan department had been rebuilt, and an institutional and retail money desk operation was started and had grown to over $200 million. *See* PX 0026 at 3, 4 and 5 (Memorandum from John M. Yunker to Larry Thrall re: Thrift Partners L.P.—Due Diligence, July 17, 1989); *see also* PX 0049 (Letter from John M. Yunker to Larry Thrall, summarizing condition of SoCal at acquisition and turn around progress through August, 1991).

The several Government regulators that testified were questioned regarding the numerous comments about SoCal's management throughout the pre-and post-breach periods that appeared in the contemporaneous Government reports. Indeed, the FHLBB exam reports and correspondence were complimentary of SoCal's management as it began the turnaround of Old Southern and the start-up of the new SoCal. For example, FHLBB acknowledged in 1988 the extensive experience of SoCal's senior management. *See*

e.g., DX 75 (Memorandum from D.A. Worthington of Federal Home Loan Bank of San Francisco to J.M. Cirona re: Credit Committee Agenda for the February 1988); PX 0207 (Memorandum from Tom C. Wilson of the Federal Home Loan Bank of San Francisco to Greg R. Reniere re: Southern California Savings Visit, Sept. 17, 1991, stating: "management has done an excellent job of running the institution. . . ."). The April 23, 1990, FDIC Report of Examination stated:

> as a workout team, current management has done well . . . . Much in the way of operating improvements and problem asset collections are attributed to him [current president, John Yunker] . . . . The chief financial officer, Jeff Kniffen, appears very knowledgeable of and most effective in dealing with accounting issues.

JX 1163 at A-1.

By June 1988, SoCal's MACRO rating had improved to 3. *See* Tr. 3610–3611(Mar). It remained a 3 after the FHLBB's targeted examination of SoCal in January 1989. *See* Tr. 447-448 (Martin); JX 1138 at 4 (Jan.1989 OTS Exam Report).

By 1989, SoCal had grown its existing branches, bringing the average branch size up from $30 million to just above $40 million in deposits, at the same time reducing branch operating expenses from roughly 95 basis points to 70 basis points. *See* Tr. 626–627 (Doyle).

SoCal President Yunker testified that SoCal was in fact *ahead* of the growth projections in the plan. Tr. 834. SoCal grew from approximately $900 million at the time of the Acquisition to approximately $2.3 billion by 1989. *See also* PX 0176 at 10 (Letter from John M. Yunker to Sidney C. Mar re: SoCal's response to the Supervisory Examination, Sept. 27, 1989). The Government's principal expert witness, Dr. William Hamm, acknowledged SoCal's growth of over one billion dollars by 1989 despite the tightening of the market, a

decline in mortgage originations, and increased competition from other California thrifts. *See* Tr. 3266-3268; *see also* DX 1108 (Graph Depicting "1-4 Residential Mortgage Originations, By Lender Group").

As of December 31, 1989, if SoCal had retained its contractual capital, its capital ratio would have been 11%, high above the 7.42% average for the 45 thrifts in California with the highest capital ratios. *See* Tr. 1387–1388; PX 0316 (Chart Depicting SoCal's Contractual Capital Ratios vs. All 182 California S & Ls—GAAP Capital Ratios as of Dec. 31, 1989, Taken from the Thrift Financial Reports). According the SoCal Plaintiffs' principal expert witness, Dr. Paul M. Horvitz, a professor of finance and an expert in the management of financial institutions, SoCal was unique in terms of the large amount of excess capital it had. *See* Tr. 4850-4851.

D. The Breach

And then came FIRREA. As then-Senate Minority Leader Robert J. Dole stated during a June 1989 White House Press Conference with President George H.W. Bush, referring to the pending legislation:

> It seems to me it's sort of a time bomb that might go off one of these days unless we have a very strong piece of legislation, stripped of all the special interests amendments, and knock out the goodwill wherever you can. There isn't much good-will for S & Ls, I find, around.

In response to Senator Dole's comments, President Bush, urging Congressional passage of his S & L legislation, now known as FIRREA, stated:

> I think that every American citizen has every right in the world to be disturbed and shocked by this situation. . . . And now some of the smaller—or the weaker S & L's, I would say, are demanding the right to continue to treat

> goodwill as capital, even though goodwill has no tangible value. And the result could be that—up to $600 billion in loans without one dollar in real capital for decades to come. And in my view, it is time for the American public and our administration to say that enough is enough.

Remarks at a White House–Congressional Leadership Meeting, June 14, 1989 (emphasis added).

Clearly, this was a high—if not the highest—domestic priority for the newly elected President. And just as clear is the fact that the Government was aware that a central aspect of FIRREA was the provision cancelling supervisory goodwill. By August 1989, Congress had passed, and the President had signed, a massive piece of legislation with far-reaching and immediate effects.

As discussed in the Liability Opinion, under FIRREA, "Congress expressly restricted the continued use of supervisory goodwill to satisfy regulatory capital requirements." *Winstar III*, 64 F.3d at 1538. FIRREA established three new minimum capital standards: "tangible" capital, "core" capital, and "risk-based" capital. 12 U.S.C. § 1464(t). After FIRREA's enactment, goodwill "could not be included at all in satisfying [the new] minimum *tangible* capital" requirements and only a certain amount of goodwill was permitted to be counted towards the new minimum core capital requirements. *Winstar III*, 64 F.3d at 1538 (emphasis added). The amount of goodwill includable in the core capital requirements was phased out entirely on December 31, 1994. *Id.* Further, the amortization period for goodwill was limited to twenty years. 12 U.S.C. § 1464(t)(9)(B).

As Mr. Yunker testified, "[e]ven though it was by stroke of pen, in the case of FIRREA, we became a troubled institution. Before that, we were very strong in terms of capital position." Tr. at 824.

Two days after the enactment of FIRREA, the OTS determined that SoCal did not meet the new capital requirements and SoCal would have to be recapitalized or face seizure. *See* Tr. at 1405-1408 (Horvitz). After a special review, August 11, 1989, SoCal's MACRO rating was downgraded from a 3 to a 4. *See* JX 1141 (OTS Special/Limited Report of Examination, Aug. 11, 1989). This rating—and the reason for the rating—continued over the next three years.

OTS promptly notified SoCal that it was a "troubled association" because it had a "substantial capital deficiency under the tangible capital requirements." *See* PX 0053 (Letter from OTS Agent Mar to SoCal Board of Directors, Aug. 30, 1989). In that letter, Agent Mar also invoked the provisions of OTS Memorandum RB 3a, which provided, as a general rule, that a troubled institution would be permitted little or no growth. SoCal had to submit a capital restoration plan that, among other things, prohibited a troubled institution from increasing its liabilities in excess of the amount of interest credited, or approximately $45 million per year. *See* PX 0049 at 1 (Yunker Letter to Thrall, Aug. 30, 1991); Tr. 945-947 (Yunker). Further, the regulators testified that SoCal had to seek OTS and later, FDIC, approval for all material transactions.

The immediate effect of the breach on SoCal was the wiping out of its regulatory capital and this led "very directly" to cessation of growth, a shrinkage of assets and liabilities, and the inability of SoCal to carry out its approved Business Plan. *See* Tr. 1401 (Dr. Horvitz).

Even taking into account all of the losses SoCal suffered prior to 1989, *absent the breach*, SoCal would have had ample capital to meet the new regulatory requirements imposed by FIRREA. *See* Tr. 1542-47 (Dr. Horvitz). In fact, as of December 31, 1989, SoCal had $258.7 million in regulatory capital. This includes the unamortized portion of the $217.5 million capital credit and $79.6 million super-

visory goodwill received as part of the acquisition. The capital requirement at that time was 3% of assets, which amounted to $70 million. Thus, SoCal had excess capital in the amount of $188 million under the previous capital definitions.

After FIRREA and its new capital definitions, SoCal had tangible capital of negative $72,000 when the requirement was $34.18 million. Thus, after the breach, SoCal had a deficit tangible capital position of approximately $34.25 million, instead of an excess of $188 million. *See* Tr. 1406-09 (Horvitz; PX 0289 (Chart Depicting Impact of FIRREA on SoCal's Tangible Capital as of Dec. 31, 1989)); PX 0295 (Chart Depicting Impact of FIRREA on SoCal's Regulatory Capital as of Dec. 31, 1989).

Core capital is essentially GAAP capital, except for some adjustment of intangible assets. Core capital is total assets minus liabilities, but certain assets such as supervisory goodwill and capital credits are deducted. FIRREA phased-out the supervisory goodwill over a period of several years until 1994. It allowed supervisory goodwill to count only up to an amount equal to 1 1/2 % of assets.

In SoCal's case this permitted retention of $34.18 million of qualifying supervisory goodwill, but that still left SoCal in a core capital deficit position of approximately $35.28 million. By 1994 the end of the FIRREA phase-out period, if nothing else changed, SoCal would have been in a negative $68.43 million core capital position. *See* Tr. 1407 (Horvitz); PX 0290 (Chart Depicting Impact of FIRREA on SoCal's Core Capital as of Dec. 31, 1989).

Risk-based capital, another FIRREA capital category, is based on a thrift's capital in terms of the riskiness of each of its assets and risk-weightings are applied accordingly. If one looked at SoCal's regulatory contractual capital as a percentage of assets, SoCal would have had a risk-based capital

ratio of 23% before FIRREA. Immediately after the breach, SoCal's risk-weighted capital would have been 3.46%, including the capital allowable during the phase-out period. After the phase-out period, SoCal's risk based capital would have been close to zero, while the risk-based capital requirement after FIRREA was 8%. Thus, instead of having a substantial surplus after the breach, SoCal was immediately in a deficit position for this kind of capital as well. *See* Tr. 1408–1409 (Horvitz); PX 0291 (Revised Chart Depicting Impact of FIRREA on SoCal's Risk–Based Capital as of Dec. 31, 1989).

We did not reach a conclusion in our Liability Opinion as to whether the breach was total or material. As with our earlier opinions, we can rely upon the conclusions of both this Court, and the Federal Circuit. As noted by Judge Christine Miller in *Hansen Bancorp v. United States*, "[i]n order to avoid proving causation, plaintiffs must establish that the [OTS] regulations constituted a total breach of the Assistance Agreement." 53 Fed.Cl. 92, 104 (2002). As the Supreme Court stated in *Mobil Oil Exploration & Producing Southeast, Inc. v. United States*:

> a breach by non-performance gives rise to a claim for total breach only if it so substantially impairs the value of the contract to the injured party at the time of breach that it is just in the circumstances to allow him to recover damages based on all his remaining rights to performance.

530 U.S. 604, 608 (2000) (quoting Restatement (Second) of Contracts § 243).

The Supreme Court in *Winstar* stated clearly that the favorable accounting treatment of supervisory goodwill and capital credits as regulatory capital were "essential to supervisory merger transactions." 518 U.S. at 849. Similarly, in two damages opinions, the Federal Circuit has stated

that the breach caused a loss of "substantial value." *Glendale Fed. Bank v. United States*, 239 F.3d 1374, 1381 (Fed. Cir.2001); *California Fed. Bank v. United States*, 245 F.3d 1342, 1351 (Fed.Cir.2001). The Court in *Hansen* concluded that the Government's breach was "total" and we agree. 53 Fed.Cl. at 104.

E. FIRREA's Impact on Operations

SoCal suffered from higher operating costs as a direct and immediate result of the Government's breach of contract due to the loss of the contract capital. Prior to the breach, SoCal was one of the most well-capitalized firms in the entire 11th District, the California geographic area in which SoCal operated, and against which the thrift compared itself. *See* PX 0316 (Chart Depicting SoCal's Contractual Capital Ratios vs. All 182 California S & Ls). After the breach, SoCal was at the opposite end of the spectrum. As the SoCal Plaintiffs' other expert, Dr. Benjamin Gerard Hartzog, testified, its capital ratio dropped to 1.45%, substantially below its regulatory capital requirement, which placed SoCal in a category of "very, very weak institutions." Tr. 1774-1775. The resulting significant drop in SoCal's regulatory capital affected three main areas: SoCal's retail and wholesale customer base, long-term strategic plans, and cost of acquiring operating capital.

First, the Government's breach affected SoCal's ability to retain and attract retail and institutional customers. Negative media attention in both financial industry publications and mass media affected the public's perception of SoCal. *See* Tr. 1775-1776 (Hartzog). SoCal had to pay higher rates in order to attract deposits from retail customers and institutional customers because of its status as a weak institution. According to SoCal's President Yunker, SoCal had to pay more for the deposits in its branches after the government's breach of contract. *See* Tr. 844. Mr. George Masa, the FDIC's regional director, also acknowledged that capital is a

factor in deposit costs and increased capital would assist an institution to keep its deposit costs down. *See* Tr. 2655-2656. SoCal management believed that SoCal's cost of deposits was 15 to 20 basis points higher than its peers due to SoCal's capital deficiency.

In addition, the loss of the contract capital adversely affected SoCal's existing wholesale, brokered, and "money-desk" deposit business. These core areas of SoCal's depositors were more sensitive to changes in interest rates, and thus more likely to abandon a failing institution. Prior to the breach SoCal had a large percentage of wholesale depositors. *See* Tr. 585 (Doyle). Many of these deposits came from SoCal's money-desk operation, which generated deposits primarily from institutional customers, such as credit unions, other savings and loans, smaller banks, and high net worth individuals. *See* Tr. 579 (Doyle).

As a result of the breach and SoCal's demotion to a "troubled" institution, SoCal could not accept any new brokered deposits or renew existing ones. *See* PX 0377 at 1 (Memorandum from John Yunker to Larry Thrall and Preston Martin: SoCal Strategy, July 18, 1990). The FDIC denied SoCal's application for permission to use brokered deposits as a source of interim funding to implement SoCal's plan to restructure the branch network. It had earlier planned to sell the northern California branches and eventually replace them with additional southern California branches. *See, e.g.*, DX 899 (Memorandum from George Masa, Regional Director to Stanley J. Poling, Director, FDIC Division of Supervision re: Southern California Federal Savings and Loan Assoc. Application for Brokered Deposit Waiver (no date)). Mr. Masa testified that the FDIC considered the risk of this strategy too excessive given SoCal's deficient level of capital. *See* Tr. 2668–2671.

Ultimately, the primary impact of the Government's breach on SoCal's cost of funds was the disruption of its plan to

expand and restructure its branch system. This was SoCal's strategic means of achieving its goal of increasing its retail deposit base. Based on his review of OTS correspondence, it is Dr. Hartzog's opinion that absent the breach SoCal would have been able to purchase branches. *See* Tr. 1777-1778. Dr. Horvitz agreed, testifying that the restrictions by the OTS on branch purchases by SoCal were "a particularly egregious example of the kind of restrictions that the OTS directive imposed on SoCal." Tr. 1419-20 (describing the regulators' decision not to permit SoCal to acquire the Santa Paula Savings branches even though it would have been good for both institutions). *See also* PX 0055 (Application to the 11th District of the OTS from SoCal requesting permission to acquire two branch offices of Santa Paula); PX 0059 (Letter from Sidney C. Mar, Assistant District Director, OTS, to John Yunker, Feb. 27, 1990, denying application for permission to the two branches, stating in relevant part: "the original proposal involves an increase in liabilities without a commensurate increase in capital by a capital-deficient institution . . . such transactions are strictly prohibited for capital-deficient institutions").

Third, we find that the Government's breach and resulting loss of contract capital affected SoCal's costs of acquiring operating capital. The breach caused SoCal to hedge more, which in turn led to higher costs for SoCal's funds. Because SoCal was unable to obtain longer term borrowings in the market after the breach, it used hedging to lengthen the term of its liabilities to make them fixed rather than variable, thereby managing its investment risk, but at a greater cost. *See* Tr. 844-845 (Yunker). Moreover, SoCal was restricted in the type of advances that it was able to obtain from the FHLBank—San Francisco because it was no longer in capital compliance.

After the breach and because of its capital position, SoCal was restricted to short term advances and could not obtain a

line of credit or other types of fixed rate longer term advances. The OTS exam reports regularly discussed problems SoCal was having as a result of its high cost of funds. *See, e.g.*, JX 1150 at 19 (OTS Report of Examination, Jan. 21, 1994); JX 1152 at Earnings-2 (OTS Report of Examination, Feb. 9, 1995). As a result of being "undercapitalized," as of May 1995, SoCal's cost of FHLBank—San Francisco borrowings was significantly higher "since the FHLB has only permitted the Association to borrow at the overnight rate rather than the lower cost of the one year rate." *See* PX 0092 at 3 (Letter from Doreen J. Blauschild, SoCal General Counsel to Timothy J. Lane, OTS Assistant Regional Director, May 25, 1995). Furthermore, the loss of capital and downgraded rating limited SoCal's alternative sources of funds, increasing its cost of borrowings under reverse repurchase agreements.

Finally, the evidence proved that SoCal was forced to incur additional expenses during the period right after the breach until 1996 that, absent the breach, it would have not had to pay. For example, while all thrifts must pay OTS filing fees and assessments, FHLBank collateral delivery fees, and SAIF (a Federal insurance fund) premiums, the evidence is uncontroverted that during this period, SoCal's fees, assessments, and premiums were higher because of its deficient capital position and low MACRO/CAMEL rating. In addition, Mr. Yunker testified at length about the fact that SoCal had to retain attorneys and financial consultants to seek advice and assistance in dealing with the regulators and in formulating new business plans to cope with the breach-induced loss of regulatory capital.

F. Efforts at Compliance with FIRREA

In this complex environment the thrift had only two options in meeting the new capital requirements. Mr. Peter Simon testified that the institution's only alternatives after the breach were either to shrink or add capital. *See* Tr. 1119-20.

A third option, to earn its way back into regulatory compliance, was impossible due to the drastic impact FIRREA had on its capital position and the accelerated timetables set forth in the new law and regulations. Accordingly, SoCal chose both alternatives in turn.

1. Shrinkage

Because of the required regulatory capital percentages, by "shrinkage," what we mean is that the thrift would dispose of assets, thereby requiring less capital as a percentage of assets. In raw numbers, "each $100 million decline in assets reduces the immediate capital needs by $3 million." PX 0116 at 1 (SoCal's CEO Report, Apr. 23, 1992).

However, because of SoCal's size, it could "not shrink fast enough, or to a size that could effectively function as an institution." Tr. 1119–20 (Simon). Mr. Yunker noted that it was not a realistic possibility for SoCal to shrink to achieve full capital compliance. Mr. Yunker described why shrinkage was undesirable:

> If you shrink to capital compliance . . . you still have the expenses and the overhead to deal with. In shrinking, you are going to sell off your best assets. Your are going to shrink your gross revenue. You are not going to correspondingly shrink your expenses. . . . You don't gain a thing by shrinking, other than getting closer to capital compliance. But in the meantime, you're effectively liquidating [or] dismantling the institution. So no, you couldn't shrink into compliance considering the deficit we had.

Tr. 859–860.

Nevertheless, as with other savings and loans impacted by FIRREA's implementation, the breach caused SoCal to shrink. This was due mainly to the strict growth and operating restrictions. Indeed, while it could not shrink its way

into capital compliance (and it would not have wanted to), the impact was felt almost immediately. Agent Mar testified that during the first quarter of 1990, "SoCal shrank by $9 million, although it had projected growth of $10.5 million during the period." Tr. 3626.

The SoCal Plaintiff's expert, Dr. Horvitz, stated that by 1995, SoCal was forced to shrink, and did in fact shrink, to a year-end low of approximately a billion and half dollars. In his words, this shrinkage had "drastic implications for the operation of the institution." Tr. 1433. Specifically, the Institutional Plaintiffs proved that there was a direct correlation between the Government's post-breach regulatory actions and its asset shrinkage. In 1990, immediately before the impact of the breach was felt, SoCal's total net assets were $2.4 billion. By 1993, the assets had shrunk to $1.8 billion. Despite this shrinkage, the core capital ratio stayed under the necessary 3.0%. Accordingly, as we will soon discuss, the thrift was required to raise additional capital to become compliant.

In 1994, the end of the goodwill phase-out period under FIRREA, the thrift again fell out of capital compliance. Accordingly, the Government issued a "Prompt Corrective Action Directive." *See* PX 0072, Apr. 28, 1994. The PCAD implemented immediate mandatory restrictions on the thrift. These restrictions limited management's rights even further than FIRREA and its regulations had with respect to transactions, assets, capital, debt management, staffing, and a number of other areas. Further, the 1994 PCAD forced SoCal to reduce its asset base even further. *See* PX 0297 (Chart With Overview of SoCal's Financial Performance and Condition).

In a May 27, 1994, letter to Timothy Lane, the OTS Assistant Regional Director, Mr. Yunker wrote:

> We received the [PCAD] by fax on April 29th. . . . We are clearly trying to avoid taking a significant loss in

> order to immediately reduce assets . . . [O]n an ongoing basis, a reduction of that size [as directed by the PCAD] would adversely impact the core earning potential of the Association. However, subsequent to the receipt of the [PCA] notice, we have begun reducing assets. . . .

PX 0073 at 1.

By 1995, SoCal's net assets totaled only $1.5 billion, a $900 million drop from the days immediately pre-FIRREA, but, capital was still insufficient to meet the regulatory requirements. *See* PX 0343 (Chart Listing Core Capital Ratios, 1987-1997).

It was not until the end of 1996 that assets began to increase and support a compliant core capital ratio of 4.58%. By 1997, assets totaled over $2.2 billion, approximately the same amount as they had been before FIRREA. *Id.* In 1998, SoCal's assets totaled $3.4 billion, and its core capital ratio was 5.38%.

The impact of the breach can also be clearly seen when measuring as a percentage the ratio of net income to assets. *See* PX 0297 (Chart With Overview of SoCal's Financial Performance and Condition). In the mid-1980's, before the Individual Plaintiffs rescued the thrift from receivership, net income to assets was as low as negative 2.95%. In 1987, it was a positive 0.06%; 1989, 0.67%; 1990, 0.60%. Immediately after the breach, the situation reversed itself again, and by 1994, net income to assets was -2.73%. It was not positive again until the end of 1996, when the ratio was +0.75%.

2. Capital Raising

a. Overview

Despite the asset shrinkage that occurred, it was not enough to bring the institution into compliance with FIRREA. Unfortunately, the nation-wide recession during 1990–1995 was not a propitious time to be entering the capital markets,

especially not on behalf of a struggling savings and loan. Messrs. Doumani, Martin, Simon, and Yunker testified unanimously as to how difficult it was to raise private capital at that time. *See* Tr. 246 (Doumani: "there was no money available"); Tr. 454-455 (Martin: it was "very, very, difficult, if not impossible, to raise private capital"); Tr. 1120 (Simon: "From the moment FIRREA was enacted, every board meeting had some very detailed discussion of the plans, the strategy to try to attract capital to our institution, talking to the various investment bankers and sole entities that might be interested in funding directly. There was a difficult environment at that time, and FIRREA made it worse."); and Tr. 849–850 (Yunker: "Savings and loans were viewed in the market as being something that people did not want to invest in, and I was unanimously told that—to forget it, that you couldn't raise capital.").

The Plaintiffs' testimony on this point was confirmed by senior OTS official Eric Shand, who acknowledged that the markets were very conservative at that time, and that it was particularly difficult for thrifts to raise capital. *See* Tr. 4135.

Despite these challenges, the Individual Plaintiffs, with the assistance of SoCal's management, formed a Board of Directors Capital Committee to seek and review various strategic alternatives with respect to SoCal's capital position. From the time of the breach, for nearly two years, however, SoCal was unsuccessful in locating any capital. *See* DX 353 at 2 (Dec. 21, 1990, Yunker letter to the FDIC: "market circumstances have been such that new capital was not and is not available."); DX 369 at 1 (SoCal's CFO Kniffin advising OTS that capital markets had "dried up for institutions in SoCal's reported financial condition," Feb. 27, 1991); and JX0995 at 1 (minutes of Feb. 22, 1991, meeting of SoCal's Capital Committee, where representative of Goldman Sachs told the Board that the "equity market for thrifts and banks has been absolutely moribund.").

Because of these problems, the SoCal Board conferred with a number of investment banking firms, including Merrill Lynch, Lehman Brothers, and as noted, Goldman Sachs. *See* PX0065 (Dec. 4, 1991 letter from William Worthington, Capital Committee Chairman, to Mr. Masa, FDIC Regional Director). Eventually, SoCal retained the firm of Keefe, Bruyette & Woods, Inc. as its investment banker to assist in capital raising efforts.

The testimony and evidence received at trial established that, as Mr. Peter Simon stated, "FIRREA was the cause of all these recapitalization needs." Tr. 1137. In all, SoCal underwent four different transactions—1992, 1995, 1997, and 1998—to raise capital. The evidence offered by the Institutional and Individual Plaintiffs and their experts is persuasive that the 1992 and 1995 recapitalizations would not have been necessary in the absence of the Government's breach. However, we find that the second two transactions, in 1997 and 1998, were not undertaken as a result of the Government's breach.

At the same time, however, it must be said that the Government's oft-repeated argument that "mismanagement" on the part of SoCal and the Individual Plaintiffs was the "overriding reason" for the recapitalizations is just plain wrong.

First, as we will discuss in a later section, it was the Government's own regulators who repeatedly issued threats of seizure through a myriad of letters, reports, and memoranda in the period after the breach, unless the Plaintiffs infused more capital. *See, e.g.*, Tr. 279-282; 312 (Doumani: "We were told that we better raise [new capital] or [we] would lose the institution" and further discussing the Government's use of the $5 million obligation in the RCMA as a "hammer" against the Plaintiffs). Second, the objective facts—the MACRO/CAMEL ratings—indicate that the thrift's capital position was directly and almost exclusively impacted by FIRREA. Third, quite contrary to "mismanage-

ment," SoCal's Board and staff did an excellent job in such a difficult financial and regulatory environment—and as the Government's reports quoted above indicate, its own regulators thought so at the time. And finally, we accept and indeed endorse Mr. Doyle's testimony that they "worked really hard at [capital raising], because [their] survival was at stake." Tr. 666.

b. First Recapitalization—1992

In 1992, after a long process of seeking new investors, Messrs. Doumani and Thrall made a successful investment offering to representatives of the Kamehameha Schools Bernice Pauahi Bishop Estate ("Bishop Estate"), a charitable educational trust established under Hawaii Law, and to BIL Securities Limited (BIL), a wholly owned subsidiary of Brierley Investments Limited, a New Zealand corporation. In July and August 1992, SCH issued $48 million in senior debt, and after payment of transaction fees and expenses, contributed $43.5 million of the net proceeds to SoCal. The result of this transaction brought SoCal into capital compliance, but just barely.

In addition to the Bishop Estate and BIL, Arbur, Inc., the Simon family trust controlled by Secretary Simon for the benefit of his children, participated in the 1992 recapitalization, 62.5% of the debt was purchased by the Bishop Estate, 31.25% was purchased by BIL, and Arbur acquired the remaining 6.25%.

However, as discussed by Mr. Doumani, the new capital providers were not content to lend SoCal money just for interest payments. Instead, they demanded an equity ownership position. *See* Tr. 245 ("This was an equity play here, and I knew of no sources that would lend us the money without an equity play."). Accordingly, SCH also issued 92,344 shares of a newly-created Class A common stock in

the same percentages to the Bishop Estate, BIL, and Arbur, for one cent per share.

The original common stock, which had no class designation prior to the 1992 transaction, was converted to Class B common stock. The preference on liquidation or sale was the preferred shareholders first, followed by payment of the senior debt, followed by payment of all SCH expenses, with the balance to be split by the common stock holders. While the number of new common shares was calculated to give the three new investors 36% of the voting rights and of the total profits upon sale, the total Class A common stock amounted to 48.64% of the total common stock of SCH.

As a result, therefore, the original common stock held by the Individual Plaintiffs was worth much less than it had been after the 1987 contract. Whereas the Individual Plaintiffs had once owned 100% of the common stock, their total ownership interest had been diluted to 51.36%. *See* PX 1202A (Common Stock Investors in SoCal Holdings Following 1992 Recapitalization). We find that this restructuring was an absolute necessity; without it, SCH would never have been able to raise funds from the new investors. Furthermore, the Government's main concern, as expressed by the regulators and as incorporated in the RCMA to have active participation by the Individual Plaintiffs, was maintained by keeping effective institutional control, but just barely, in the hands of the original contract signatories. Following the consummation of this transaction, the OTS terminated the RCMA. *See* JX 1506 (Conditional Termination of the RCMA, Irrevocable Proxy and Dividend Limitation Stipulation, June 30, 1992).

To infuse the cash directly into SoCal, SCH purchased 435,000 shares of "Series B Non-Cumulative Perpetual Preferred Stock." That stock was senior to the original preferred stock of SoCal, which was owned by Memvale, FIMA, and SCH after the 1987 contract was signed. Since it was

non-cumulative and perpetual, it was permitted to count as core capital for regulatory reporting purposes. *See* PX 0036 (Oct. 19, 1992, Memorandum from Jeff Kniffin to Files re: 1992 Capital Restructuring).

This FIRREA-induced recapitalization had additional costs. First, the SoCal Plaintiffs paid $5.218 million in transaction costs. Second, the notes that were issued were very expensive, in terms of the interest rate on the notes. During years 1-8, the notes bore interest at 15% per annum; in year 9, 17%; and in year 10, 19%, all payable in quarterly installments. SoCal attempted to pay less interest, "but there wasn't capital available" that would take less than that. *See* Tr. 975 (Yunker). The Government regulators recognized at the time of 1992 recapitalization that it was expensive, but necessary. Agent Mar testified that the "high yield promised to preferred stockholders [and the] high costs of debt" was an additional cost of the capital raised. Tr. 3675-76. And in an October 1993 report George Masa, another of the regulators, wrote that:

> "SoCal's capital position was markedly improved with a $42.2 million recapitalization in August, 1992. . . . [SCH] financed the capital injection through issuing high cost subordinated debt (written at 15 percent and escalating to 19 percent) to non-Simon investors. Dividend payments from SoCal are the holding company's sole source of income. From 1993 to 1997, debt service will run $6 million/annually."

DX 594 (Memorandum from Mr. Masa to Mr. Stone, Oct. 23, 1993).

Despite over $5 million in transaction costs and required interest payments of over $500,000, and the costs of diluted ownership borne by the Individual Plaintiffs, the recapitalization worked—for a time. *See* PX 0042 (Jan. 26, 1993, Update Memo to Files from Jeff Kniffin); PX 0282 (Cost of

1992 Senior Notes). Immediately after this transaction, on November 16, 1992, SoCal's CAMEL rating was a 3, and its core capital ratio was over 3% for the first time since the breach. And while the thrift was capital compliant with the current requirements immediately following the 1992 capital infusion, FIRREA imposed increasingly stringent capital requirements as the Act went fully into effect, and the thrift had to meet these requirements. Thus, it remained a 3 for only one year—by November 1993, it was again rated a 4.

c. Second Recapitalization—1995

The harmful effects of the breach continued to build from 1992 to 1995. Notwithstanding the over $43 million in new capital that was infused in 1992, SoCal's capital position was not sufficient to absorb the significant credit losses which continued to mount. In 1995, a second recapitalization became necessary.

The Court heard considerable testimony about the effects of the recession in California, the worst since the Great Depression; about the massive decline in real estate values; and about the losses which stemmed from the riots in Los Angeles following the Rodney King trial and Northridge earthquake in 1994. Nonetheless, we find that FIRREA was the principal cause of this additional round of capital raising. As Mr. Yunker stated, while the 1992 capital raise "just barely" "filled the hole," the regulators "still wanted additional capital." Tr. 855, 861. Interestingly, as noted in PX 0088, an April 7, 1995, letter (prior to the 1995 recapitalization) from SoCal to the OTS, "If SoCal was permitted to include [the qualifying supervisory goodwill booked in 1987] . . . as of March 31, 1995, it would be deemed well-capitalized as of that date."

As discussed above, SoCal received the April 1994 Prompt Corrective Action Directive, and was specifically told that it would "not survive without an immediate and substantial

capital infusion." JX 1168 (the 1994 year-end FDIC Report of Examination, Nov. 28, 1994, which indicated that absent new capital, "closure . . . is anticipated"). By the end of 1994, the end of the supervisory goodwill and capital credit phase-out period, the thrift had again fallen out of regulatory capital compliance. *See* PX 0264 (Letter from John Yunker to Timothy Lane, Jan. 27, 1995, stating that the final regulatory phaseout of goodwill rendered SoCal "critically undercapitalized").

Thereafter, the OTS placed SoCal in the Accelerated Resolution Program of the Resolution Trust Corporation (RTC) (created by FIRREA to dissolve failing thrifts and liquidate their assets and assume their liabilities). *See* PX 0084 (Agreement between SoCal and OTS). In a final sign of SoCal's imminent potential for failure and seizure, in November 1994, it was assigned a composite rating of 5. *See* PX 3148 (OTS Letter to SoCal Board of Directors).

As in the first recapitalization, the Individual Plaintiffs, together with the Board and management, actively sought additional investors and capital. The capital markets in 1995 were as tight as they were in the 1990-1992 period after FIRREA. Accordingly, the Board of Directors, with the Government's concurrence, turned again to the 1992 capital providers for additional funds. *See* JX 1168 (FDIC's 1994 year-end report which noted how difficult it was for SCH to raise capital, stating that the 1992 capital providers "constitute the only potential source of additional funds at this time.").

In June of 1995, SCH raised $60.5 million in capital by issuing debt and equity. The capital providers, however, would only agree to invest additional cash into SoCal if the Individual Plaintiffs' remaining ownership interest were extinguished, and if the Board brought in new management. *See* JX 24 (SoCal 1995 Annual Report); Tr. 245–47 (Doumani: "those were the terms. At that particular time,

there was no money available. . . ." other than going to the 1992 capital providers). In the view of Mr. Peter Simon, no other form of capital was available—the only source of funds was the entities that had participated in 1992. *See* Tr. 1135. The testimony and evidence of the other Individual Plaintiffs, SoCal management, and significantly, of the Government's regulators, support Mr. Simon's conclusion and we agree.

Further, in connection with, and as a prerequisite to the 1995 recapitalization, the Individual Plaintiffs' shares of SCH common stock purchased in the 1987 acquisition transaction were cancelled for no consideration. This demand, and SCH's acquiescence to it, was specifically reported to and approved by the Government:

> The shareholders of SCH have been advised by Bishop, Brierley and Arbur that they are willing to invest the funds in SCH necessary to recapitalize the association if and only if a plan of reorganization in substantially the following form is implemented. . . . [T]he outstanding shares of SCH Class B Common shall be cancelled without consideration.

See JX 1607 (Letter from SoCal General Counsel Doreen Blauschild to Timothy Lane at OTS, transmitting SCH corporate resolutions adopting the June 1, 1995, Plan of Reorganization); *see also* JX 1619 (1995 Recapitalization Closing Memorandum); JX 1620 (Agreement and Plan of Reorganization); JX 1599 (Letter from Gerald L. Hawkins, attorney for SCH, to John F. Robinson, OTS Regional Director, Apr. 20, 1995, confirming the Government's approval of the recapitalization).

Each Plaintiff's witness and several regulators testified that the management team from 1989–1995 had done an excellent job, and were, in the words of one of the Individual Plaintiffs "very strong" and "very competent." Tr. 1138 (Simon). However, the management transition required as a part of the

1995 recapitalization occurred in March 1995. SoCal replaced its former senior managers, including Messrs. Doyle and Yunker, with a new management team with considerable experience in commercial banking and problem asset resolution. The new management team included Rudolph P. Guenzel as President and CEO, and J. Michael Holmes as Executive Vice President and Chief Financial Officer. It was important to have leaders with experience in this area because of SoCal's new business plan to transition the thrift to commercial bank-type operations.

Mr. Holmes testified that the crux of the new management team's strategic plan was the infusion of additional capital. *See* Tr. 1235. Accordingly, the second recapitalization was executed in June 1995. In this transaction, the 1992 capital providers were again the sole participating entities. The Senior Notes issued in 1992 were returned to SCH and contributed to the capital of SoCal. In addition, the Bishop Estate and BIL purchased $10 million in new debt, bearing an initial interest rate of 7% per annum, increasing in increments to 10.75% and eventually to 11.15% per annum. SCH also issued a $2 million Senior Note to Arbur.

In equity, as noted, SCH cancelled for no consideration the shares held by the original contract signatories, the Individual Plaintiffs. Various outstanding series of the preferred stock issued in 1987 were redeemed (that held by Memvale and FIMA), and the preferred stock issued in 1992 was exchanged for Common Stock. SCH also issued 85,000 of Series C Preferred Stock, 68,000 in Series D Preferred Stock, and 332,000 in Series E Preferred Stock. Each of these Series required quarterly dividend payments of $2.95, $3.00, and $3.00 per share, respectively. For the equity, SCH received $48.5 million.

As a result of this transaction, SCH infused $60.4 million of capital directly into SoCal. The SoCal Plaintiffs incurred over $700,000 in transaction costs from raising this capital,

and were required over the next several years to make dividend and interest payments of over $22 million on the equity and debt issued in 1995. *See* PX 0283 (Cost of 1995 Senior Notes); PX 0284 (SoCal Plaintiffs' 1995 Recapitalization Expenses).

The remaining common shareholders in SCH following the 1995 recapitalization were the Bishop Estate, with 60% of the shares; BIL, with 30% of the shares; and Arbur, with 10% of the shares. Messrs. Doumani, Martin, Simon, and Thrall were each left with nothing, and, similarly, all of Arbur's original 1987 investment was cancelled. The Individual Plaintiffs and their experts refer to this 1995 transaction as "dilution-to-zero." It is more properly called "extinguishment."

By August 1995, shortly after this transaction, SoCal was raised to a composite 4 rating. Throughout two subsequent examinations, a regular one in February-March 1996, and a SoCal-requested special exam in September 1996, the OTS continued to give the institution a CAMEL composite rating of 4. *See* JX 1153 (OTS Report of Examination, April 12, 1996); JX 1155 (Memorandum from Richard Kuczek, Regional Examiner to Timothy Lane, Sept. 25, 1996). Despite the recent infusion of over $60 million, and despite pleas during both examinations by SoCal's management, the regulators specifically declined to upgrade SoCal's rating.

However, the situation changed during its next regular examination, which concluded in April 1997, and evaluated SoCal as of December 31, 1996. After that review, the examiner concluded:

> After the recapitalization of SoCal in June 1995 and installation of new management, the Bank set on a course of improving earnings, capital, and asset quality. The primary steps were control of general and administrative (G & A) expenses and the disposal of problem

> assets. . . . These accomplishments contributed to the Banks' positive 1996 earnings, the first year of positive earnings for the Bank since 1992.

JX 1157 (OTS Report of Examination, April 29, 1997).

The OTS scored SoCal a 3 in every CAMEL category (capital adequacy, asset quality, management, earnings, liquidity) and a 4 in sensitivity to market risk. Overall, though SoCal was rated a 3. We conclude that at this time, as of December 31, 1996, the institution was restored to a healthy capital position, recovering the "3" it had on the eve of FIRREA's passage. The effects of the Government's breach had thus been mitigated by the considerable efforts of the institutional and Individual Plaintiffs and, of course, by the infusion of approximately $100 million in tangible capital. SoCal was finally out of the very deep hole it had been in for years.

d. Two More Transactions—1997 & 1998

The Institutional Plaintiffs also claim damages arising out of the third and fourth transactions to infuse additional capital into SoCal. They assert that OTS continued to pressure SoCal even after the 1995 recapitalization to raise yet more capital. *See* JX 1153 (OTS Report of Examination, April 12, 1996, where OTS notes that it encouraged the Board to attain "well capitalized"—CAMEL 1 or 2—status). This may well be the case. However, we find that the transactions that SoCal undertook following its return to a composite 3 rating in early 1997 were independent business decisions that were not undertaken to replace the capital lost as a result of the breach.

To be sure, the 1997 and 1998 transactions were "capitalizations"—in that they both resulted in additional capital for the thrift. But the Court declines to find that they were "recapitalizations" necessary to replace the contractual capital lost as a result of FIRREA.

With the arrival of the new management team, SoCal retained the investment banking firm Sandler O'Neil & Partners. Thereafter, in 1997, SoCal formed People's Preferred Capital Corporation (PPCC), a real estate investment trust (REIT). PPCC, in turn, issued 1.4 million shares of Non-cumulative Exchangeable Preferred Stock bearing a 9.75% dividend, with a liquidation preference of $25.00 per share. *See* PX 0140 (PPCC Prospectus, Sept. 30, 1997). This REIT transaction raised $35.65 million in gross proceeds, $33.25 million of which was contributed upstream to SoCal and counted as regulatory capital. SoCal paid $2.4 million in transaction costs, and PPCC paid $14.7 million in dividends on the preferred stock it issued. *See* PX 0308 (Cost of 1997 REIT Transaction).

One year later, SCH (now called PBOC Holdings, Inc.) conducted an Initial Public Offering (IPO) of the common stock of SCH. *See* PX 0141/JX 1804 (PBOC Holdings, Inc. Prospectus, May 12, 1998). In connection with the IPO, SCH paid all accumulated dividends on its previously issued and outstanding Series C, D, and E Preferred Stock. Further, it also redeemed this preferred stock in exchange for 8.5 million shares of SCH common stock. In doing so, it incurred a cost of $68.753 million, representing the cost of conversion (the value of 8.5 million common shares times the $13.75 price per share, less the $48.5 million face value of the preferred stock). *See* PX 0287 (Cost Notebook/Exhibit E: 1998 Recapitalization). The IPO cost SCH $10.593 million in transaction costs. *See* PX 0309 (Costs of 1998 Recapitalization). The company's common stock was approved for quotation on the Nasdaq National Market and was listed under the symbol PBOC.

The IPO was priced at $13.75 per share of common stock. It is significant to note that the allotment was comprised of shares offered by both the holding company and the existing common stock holders (at that time, Bishop, BIL, Arbur).

The net proceeds for SCH totaled approximately $129 million, of which approximately $88 million was infused into SoCal as paid-in capital. *See* PX 0391 (Memorandum from J. Michael Holmes to George Limm, OTS Examiner, July 8, 1998).

In that 1998 memorandum, Mr. Holmes noted that the IPO had three objectives: first, to "clean up" the capital of the holding company by "eliminating high-cost senior debt and cumulative preferred stock"; second, to raise additional capital to support growth; and third, to increase SoCal's regulatory capital ratios. *Id.* While the Court appreciates and understands SoCal continued need to expand its capital position, we do not find that the breach was the substantial factor in causing either the 1997 or the 1998 transactions.

One final note: in April 2001, the Institutional Plaintiffs announced that they had entered into an agreement with FBOP Corporation (FBOP), a savings and loan holding company incorporated in Illinois. The merger was consummated in November 2001, and provided for the conversion of each share of SCH common stock into the right to receive $10.00 per share. FBOP is an $11 billion multi-state holding company and the parent company of California National Bank (CNB). The successor-in-interest to SoCal, CNB has 59 branch locations in California and assets of over $6 billion. *See* www.fbopcorporation.com/about_ us.html.

G. Additional Findings with Respect to the Individual Plaintiffs

1. Simon/Arbur Relationship

Though the Simon Plaintiffs—Arbur and now the Estate of William E. Simon, Sr.—have two identities, we find that throughout their relationship with the Government, and in their operation and management of SoCal, they were in reality one entity controlled by Secretary Simon until his

death. This sub-section discusses several additional facts specific to the Simon Plaintiffs.

Mr. Peter Simon testified that his father sold his shares of common stock in SCH to Arbur on October 4, 1989 for the "nominal amount" of $19,400, or $1 per share. Tr. 1140; *see also* DX 260 (Stock Purchase Agreement between Arbur, Inc. and William E. Simon, Sr., Oct. 4, 1989). Arbur, as we have said, is a closely held family corporation, owned solely by members of the Simon family, and organized for the benefit of Secretary Simon's children. Mr. Peter Simon characterized this transfer as "pure and simple estate planning" done without regard to SCH, SoCal, or even FIRREA. Tr. 1140. At the time, the elder Simon had the controlling vote in Arbur, but a very small percentage of its overall ownership. Many of Secretary Simon's other personal and marital holdings were also transferred to either Arbur or to the Simons' charitable foundation as well. *Id.*

Mr. Tomas E. Randlett, a certified public accountant and one of the experts called upon by the Government to testify about cash flow accounting at SCH and SoCal, believes that for purposes of assessing both cash flow and the damages suffered by the Simon Plaintiffs, it is appropriate to view Secretary Simon's interests together with Arbur's. *See* Tr. at 3922–3923. Clearly, the transfer of Mr. Simon's interest to Arbur did not dilute the Simon Plaintiffs' collective interest.

The evidence clearly established that Mr. Simon's transfer of his individual ownership interest to himself and his children as the sole owners of Arbur represented a change in form, not substance. Moreover, despite the Government's attempt to characterize the transfer as "arm's length," it was not. *See* DX 259 (Memorandum from William E. Simon, Jr. to William E. Simon, Sr. re: Sale of SoCal Holdings, Inc. Common Stock to Arbur, Oct. 3, 1989). We agree with the Simon Plaintiffs' characterization of this transaction as a transfer done for estate planning purposes. Accordingly, the

Court will analyze the economic harm to Secretary Simon caused by the Government's breach, and the damages necessary to redress that harm, together with the harm and damages for Arbur.

After 1989, and before 1995, Mr. Peter Simon stated that there was no further transfer of these shares, and no additional compensation was received for these shares. *See* Tr. 1140. The entire 29,000 shares acquired by the Simon Plaintiffs in 1987 were cancelled for no consideration in the 1995 recapitalization. Neither Secretary Simon nor his Estate have ever received a penny for the loss of those shares.

Arbur, as we have said, participated in the first two recapitalizations. It gave new consideration for the newly issued SCH shares in both 1992 and 1995. In 1992 the Simon Plaintiffs invested $2.88 million in an SCH senior note. *See* PX 1205A (Simon Plaintiffs' Investments in SoCal Holdings). Also in connection with their participation in the 1992 recapitalization, the Simon Plaintiffs received 5,771 SCH Class A common shares, which were issued at one cent per share. *See* PX 1202A (Common Stock Investors in SoCal Holdings Following 1992 Recapitalization); JX 1526 (Stockholders' Agreement Among SCH, the Common Shareholders, Bishop, BIL Far East and Memvale, July 28, 1992).

In 1995, the Simon Plaintiffs again assisted SCH with its mitigation efforts by participating in the second recapitalization. In that transaction, the Simon Plaintiffs invested $4 million in SCH series D preferred stock and invested another $1.92 million in an SCH senior note (pursuant to a contractual commitment made during the 1992 recapitalization). *See* PX 1205A (Simon Plaintiffs' investments in SoCal Holdings); JX 1619 (Closing Memorandum, June 1, 1995).

Mr. Peter Simon persuasively testified that the Simon family, through Arbur, participated in the 1992 and 1995 recapitalizations "for confidence's sake." Tr. 1135-36. He

contended that the Simon family, as an existing investor, was compelled to purchase additional shares in SCH to entice new investors who otherwise would not have participated in these offerings without the imprimatur of an existing owner's (who also happened to be a former Secretary of the Treasury) continued confidence in SoCal's future. *Id.*

Arbur sold its new SCH securities, unrelated to the Simon Plaintiffs' initial investment interest, in the 1998 IPO and 2001 merger. As part of the IPO, the Simon Plaintiffs received a $1.6 million preferred dividend and sold a portion of their SCH stock—all of which was acquired after the Government breached its contract—for which they received approximately $4.9 million. *See* JX 1796 (Correspondence Re: Payment of Dividends and Proceeds of Sale of Stock to Selling Stockholders). Following the IPO, the Simon Plaintiffs retained ownership of additional shares of SCH common equity. *See* DX 867 (Letter from J. Michael Holmes to Mark Butler re: IPO Over–Allotment Settlement, May 19, 1998).

As part of the merger with FBOP Corporation, the Simon Plaintiffs surrendered their remaining SCH shares and received proceeds—all of which were traceable to the 1992 and 1995 SCH investments—in the approximate amount of $6.4 million. *See* PX 1205A (Simon Plaintiffs' Investments in SoCal Holdings).

The Simon Plaintiffs could not and did not sell the shares it acquired pursuant to the 1987 contract with the Government because those shares were cancelled without consideration in 1995 as a direct consequence of the Government's breach. We find that any benefit that accrued to Arbur upon disposition of those new securities in no way compensated the Simon Plaintiffs for elimination of their pre-breach, contractual interests.

2. Individual Plaintiffs "Divorce" from Ariadne

In 1990, the Individual Plaintiffs and the Ariadne entities went through "a very complex divorce, a financial divorce with Ariadne. . . ." Tr. at 1142 (Simon). *See* DX 305 (Letter from Madeleine A. Kleiner of Gibson, Dunn and Crutcher to Ed McManus of OTS summarizing the principal elements and components of the financial divorce between the Simon interests and Ariadne, May 15, 1990).

Aspects of the 1990 "divorce" between the Individual Plaintiffs and Ariadne included, among other things, (a) payment of $32 million from the Simon family to Ariadne, (b) transfer of certain real estate interests, (c) exchange of mutual releases, (c) increase in the loan to the Individual Plaintiffs to purchase and hold SCH stock from $5.8 million to $30 million and conversion from recourse to non-recourse, (d) a new $6 million loan from the Simon family to Ariadne, (e) pledge of the SoCal note by Ariadne to the Simon family to secure the $6 million Ariadne note, and (f) other terms. *See, generally,* Tr. 1142-1154 (Simon); DX 59 (Letter from Gerald Parsky to David Crawford of Peat Marwick Hungerfords in care of Ariadne Australia Limited, Dec. 16, 1987); DX 63 (Letter from Gerald Parsky to Anthony Thomas, Ariadne Australia Ltd., Jan. 8, 1988); DX 88 (Letter from Gerald Parsky to Eugene Cafiero, KDI Corp., Mar. 31, 1988); JX 1543 (Amended and Restated Promissory Notes from each of the Common Shareholders in favor of Memvale, July 6, 1990).

The 1990 restructuring had little, if anything to do with SoCal or the economics of that transaction and was admittedly not caused by the Government's breach. *See* Tr. 1178–1179 (Mr. Simon testifies that the financial divorce with Ariadne was unrelated to SoCal or the Government's breach). As we discuss later, the Government's argument that the Individual Plaintiffs suffered no harm as a result of the restructuring of their loans from Ariadne has no merit.

3. Thrall/Arbur Relationship

Mrs. Beverly Thrall testified that she and her husband, Larry Thrall, were in a very bad financial condition in the early 1990's. *See* Tr. 489. As noted, Mr. Thrall had borrowed extensively to invest with the Simon family in several other thrifts. When FIRREA caused a precipitous decline in the value of his banking investments, the Thrall[s'] personal financial condition was negatively impacted.

Accordingly, on October 16, 1992, Mr. and Mrs. Thrall executed an omnibus Transfer Agreement with Secretary Simon. *See* PX 3131 (Transfer Agreement by and between Larry B. Thrall and William E. Simon, Sept. 30 and Oct. 16, 1992). In the 1992 Transfer Agreement, the Thralls settled their debts by transferring their holdings in the various savings and loans to various entities to whom they owed money. *Id.* Their 14,000 shares in SCH (at this time, they were already impaired by the breach and diluted by the first recapitalization) were transferred to Arbur.

We find that this transfer would not have been necessary but for the Government's breach. As Mr. Thrall's co-Plaintiff and business partner, Roy Doumani stated:

> [T]here would not have been a need [for Mr. Thrall to transfer his shares to Mr. Simon], because the asset and the coverage that that asset gave for the money that had been borrowed from Mr. Simon by Larry was more than adequately covered [before the breach].

Tr. 240-41.

And yet, despite the transfer, Mr. Thrall did not walk away from SoCal. Mrs. Thrall's testimony made it clear that Mr. Thrall was committed to SoCal, and to honoring his commitment to the Government in the RCMA.

> Larry was very much vested in [SoCal's] future and its success. After the breach he was horrified and dismayed

> . . . He just kept saying, this is just a disaster. How could they do this? I mean, don't they realize what they have done? [He] became almost obsessed with trying to figure out how can they make this work, even though the contract had been breached. . . [H]e was working day and night, honestly, trying to work that out. . . . And ultimately, he became very depressed, and his health suffered. . . . [I]t really was a horrible problem for him.

Tr. 479–81.

The undisputed testimony of SoCal's senior managers, and of the regulators, was that Mr. Thrall was one of the leaders in seeing to it that SoCal was adequately recapitalized after FIRREA. *See* Tr. 217 (Doumani); Tr. 985 (Yunker); *see also* JX 0308 (Minutes of SoCal Board of Directors Meeting, Sept. 25, 1990). SoCal President Yunker stated:

> Larry Thrall . . . was taking the lead, for the most part, relative to the shareholder efforts [to raise capital]. . . . [Mr. Thrall] was under an incredible amount of pressure to assist in the raising of capital, and Larry felt personally responsible for the fact that the deal wasn't working out.

Tr. 852, 988.

In sum, the evidence is clear that like his partners, Mr. Thrall was committed to SoCal and he would not have transferred his interest if it had not been absolutely necessary in the wake of FIRREA.

IV. *Damages Standards*

Winstar damage claims have been the subject of many recent opinions. The judges of this Court and of the Federal Circuit have encountered the various *Winstar* plaintiffs' damages theories, and the Government's defenses to them, several times. We summarize our understanding of the guidelines expressed in the Federal Circuit's opinions in the following

cases: *Glendale Fed. Bank v. United States*, 239 F.3d 1374 (Fed.Cir.2001); *California Fed. Bank v. United States*, 245 F.3d 1342 (Fed.Cir.2001); *Bluebonnet Sav. Bank v. United States*, 266 F.3d 1348 (Fed.Cir.2001); and *LaSalle Talman Bank v. United States*, 317 F.3d 1363 (Fed.Cir.2003). Each of the damage claims before us was before the Federal Circuit Court in one or more of those cases. Accordingly, we turn to them as our analytical starting point.

A. Expectancy Standards

There are three general categories of contract damages—expectancy, restitutionary, and reliance damages. As the Federal Circuit has noted, "one way the law makes the non-breaching party whole is to give him the benefits he expected to receive had the breach not occurred." *Glendale*, 239 F.3d at 1380 (citing Restatement (Second) of Contracts § 344(a)). These expected benefits are "often equated with lost profits," though they "can include other damage elements as well." *Id.* Lost profits are a "just and proper item of damages, to be recovered against the delinquent party upon a breach of the agreement . . . if the profits are such as would have accrued and grown out of the contract itself, as the direct and immediate results of its fulfillment." *Energy Capital Corp. v. United States*, 302 F.3d 1314, 1328 (Fed.Cir.2002) (quoting *Wells Fargo Bank v. United States*, 88 F.3d 1012, 1022-1023 (Fed.Cir.1996)).

In terms of proof, the Circuit has stated that "[e]xpectation damages are recoverable provided they are actually foreseen or reasonably foreseeable, are caused by the breach of the promisor, and are proved with reasonable certainty." *Bluebonnet*, 266 F.3d at 1355 (citing Restatement (Second) of Contracts §§ 347-351). The Federal Circuit has further held that the standard for causation is that the breach must be a "substantial factor" in the damages, not the "but for" cause of the plaintiff's harm. *Id.* at 1356.

There are two important observations when it comes to *Winstar* expectation damages. First, we learned from the *CalFed* opinion that "[b]oth the existence of lost profits and their quantum are factual matters that should not be decided on summary judgment if material facts are in dispute." 245 F.3d at 1350. Thus, in that case, the Federal Circuit directed the U.S. Court of Federal Claims to hold a trial to find the facts relative to those claims. Second, to date, no trial court has awarded lost profits in a *Winstar*-related case, at least not to an open bank or holding company. In the *Glendale*, *LaSalle Talman*, and *California Federal* cases, the trial courts held that the plaintiffs did not meet their burden of proof for lost profits. For much the same reasons we come to the same conclusion in this case.

B. Restitution Standards

A second category of contract damages is restitutionary relief. According to the Restatement, restitution is the plaintiff's "interest in having restored to him any benefit that he has conferred on the other party." Restatement (Second) of Contracts § 344(c). One measure of restitution is the "value of the benefits received by the defendant due to the plaintiff's performance." *Landmark Land Co. v. United States*, 256 F.3d 1365, 1372 (Fed.Cir.2001). In other words, restitution is a remedy that sounds in disgorgement—it takes from the breaching party the benefits conferred on him, and it returns the "non-breaching to the position it would have been had there never been a contract to breach." *Glendale*, 239 F.3d at 1380.

In the *Winstar* context, thrifts seeking restitution (as opposed to investor-signatories) are seeking the cost savings to the FSLIC for not having to liquidate the acquired institution. To do so, the thrift plaintiffs seek the estimated amount of liquidation costs (generally, there are two estimates—a plaintiff's estimate and the original Government estimate from the time the contract was signed) less any FSLIC cash assistance

or FSLIC indemnification payments. This is said to be the amount of the Government's benefit it should not keep in light of the later breach.

At the conclusion of the first *Winstar* damages trial, then-Chief Judge Smith awarded the *Glendale* plaintiffs "restitutionary" damages, calculated in terms of the liabilities of the troubled thrift that were assumed by the plaintiff in the supervisory acquisition. 43 Fed.Cl. 390 (1999). The theory was based on an argument that the Government did not have to assume those liabilities, or pay that amount, from the insurance fund upon the hypothetical future liquidation of the thrift. The Federal Circuit, however, overturned that award. While it noted that promises in *Winstar*-related contracts have "substantial value," it stated that:

> the action taken by the purchasing S & L in acquiring the failing thrift did not result in the Government, specifically the FSLIC, saving the dollar value of the net obligations of the thrift.
>
> In a very real sense, what the Government received in exchange for its promise was time—time to deal with other failing S & Ls, time to see what the market would do before having to commit substantial resources to the problem.
>
> It is important to remember that, even after [the merger], the Government was not free of potential liability for the failing thrift. Had interest rates not come down... [and the thrift failed], the Government's contingent liability would have matured.

Glendale, 239 F.3d at 1382.

Thus, the Federal Circuit held that damages could not be measured in terms of a "liability that never came to pass, and based on a speculative assessment of what might have been. . . ." *Id.* The Institutional Plaintiffs' restitutionary

claim as measured by the cost savings to the FSLIC is similarly defective.

C. Money–Back Restitution Standards

Another measure of restitution damages in the *Winstar* context applies to the plaintiffs who are individual contract signatories. These plaintiffs participated as individuals in the transactions, were parties to the various instruments that formed the binding contract, and are shareholders of either the thrift or its holding company. As independent parties to the contract, they are entitled to damages for harm they suffered by the Government's breach of promises to them and independent of harms suffered by other parties to the contract.

Awarding damages to these plaintiffs requires a case-by-case analysis of the pre-and-post breach events and how they affected their individual interests. In general, however, several courts have held that they are, at a minimum, entitled to "money-back" restitution for their initial investment in the thrift. *See Mobil Oil*, 530 U.S. at 608; *Hansen Bancorp*, 53 Fed.Cl. at 100 (2002). On the other hand, the individual shareholders may be limited in their ability to claim such things as dimunition, or expectancy, damages. *See LaVan v. United States*, 56 Fed.Cl. 580 (2003).

If the trial court finds that the harm and injury to the individual plaintiffs is "separate and distinct" from the harm to the institution, the court may award damages over and above the simple award of money-back restitution. *See LaSalle Talman Bank v. United States*, 45 Fed.Cl. 64, 73 (1999); *Strougo v. Bassini*, 282 F.3d 162, 172–75 (2d Cir. 2002); 12B FLETCHER CYCLOPEDIA OF THE LAW ON CORPORATIONS § 5913 (2000). Accordingly, in specific application, the Federal Circuit has held that an individual investor plaintiff is entitled to compensation "based on the profits [he] relinquished" when a breach-induced recapitalization forces

him to "give up a significant equity stake." *Bluebonnet*, 266 F.3d at 1356.

Determining that compensation is a matter for the trial court, and where the fact of damage is proven, "it is not essential that the amount thereof be ascertainable with absolute exactness or mathematical precision." *Id.* at 1355. We take this approach with respect to the Individual Plaintiffs, and we note at the outset that their damages claim does permit the Court to award damages based on a concrete number, and not upon a hypothetical theory or construct.

D. Reliance Standards

A third category of damages is known as reliance damages. The principle of reliance damages is that a party who relies on another party's promise made binding through a contract is entitled to damages for any losses actually sustained as a result of the breach of that promise. See *Glendale*, 239 F.3d at 1382–83. "The reliance recovery is a reimbursement for losses the plaintiff suffers in reliance on the defendant's contractual promise." *3* DAN B. DOBBS, LAW OF REMEDIES § 12.3(1) (2d ed.1993). As a general matter, reliance damages are available for costs incurred both before and after the breach.

In the *Winstar* context, the plaintiffs typically seek three types of reliance damages, two of which have been generally accepted to date by the Federal Circuit. Because the term "reliance" is so broad, for the purposes of the trial in this case, the Court adopted the generally-agreed upon *Winstar* nomenclature for these three areas of damages—"Wounded Bank" Damages, Replacement of Lost Capital, and Assumption of Liabilities.

The first type of reliance damages are so-called "*Wounded Bank* " damages. "Wounded bank" damages are costs incurred by the thrift because of its status as a "troubled" or under-capitalized institution—a status directly related to

FIRREA's mandated removal of goodwill from the thrift's regulatory capital. *Winstar* plaintiffs claim as "wounded bank" damages the following types of costs—higher costs of funds, higher insurance and regulatory premiums and assessments, and extra attorney and consultant fees to interface with the regulators.

The trial court in *Glendale* awarded "wounded bank" damages. On appeal, the Federal Circuit did not review the underlying data on the individual areas, but after reviewing and noting the specific damages, stated:

> [W]e conclude that, for purposes of measuring the losses sustained by Glendale as a result of the Government's breach, reliance damages provide a firmer and more rational basis than the alternative theories argued by the parties.

Glendale, 239 F.3d at 1383.

We found that also to be the case in this trial.

The second type of reliance damages for thrift plaintiffs is the *Cost of Replacement Capital*. In a *Winstar* context, this is the damage theory that is the easiest to understand, and easiest to quantify. Simply stated, it is the amount of money spent by the thrift to replace the goodwill lost as a result of the government's breach. This can include transaction costs and related capital-raising expenses. Because contract law precludes recovery for speculative damages, this category of damages has been repeatedly adopted by the trial judges, and endorsed by the Federal Circuit. *See, e.g., Bluebonnet*, 266 F.3d at 1356 ("The Court of Federal Claims properly determined that the breach of the forbearances was a substantial factor in Blunebonnet's increased financing costs because it forced Bluebonnet to raise capital when FIRREA had made investments in thrifts riskier and considerably less attractive."). We do so here, as well.

In *LaSalle Talman*, the plaintiffs sought the cost of replacement capital. While the trial court rejected the specific costs claimed based on a hypothetical construct which was also later rejected by the Federal Circuit, Judge Bruggink stated the following:

> [T]he cost of replacement capital can serve as a valid theory for measuring . . . damages in the *Winstar* context because it provides a measure of compensation based on the cost of substituting real capital for the intangible capital held plaintiff in the form of supervisory goodwill.

45 Fed.Cl. 64, 87 (1999).

In response, the Federal Circuit concluded "we agree with these statements of principle. . . ." 317 F.3d at 1374.

In a similar case that went to trial on this type of damages claim, Judge Hodges also explained the rationale behind the "cost of replacement capital theory:"

> The Government's breach resulted in the elimination of CalFed's supervisory goodwill. CalFed is entitled to what it would cost to replace that goodwill in the capital market.

43 Fed.Cl. 445, 460 (1999).

Accordingly, Judge Hodges awarded the CalFed plaintiffs their claimed transaction or "flotation" costs. The Federal Circuit, on appeal, found "no clear error in the [Court's] factual finding that the flotation costs provided an appropriate measure of CalFed's [cost of replacement] damages. . . ." *CalFed*, 245 F.3d at 1350. Transaction costs include such items as investment bankers, attorneys and consultant fees, and other expenses actually incurred and paid that were related to the issuance of equity and debt.

Such costs are not limited to the "flotation costs" of raising that new capital, but can also conclude obligations incurred on issuing that capital. The Federal Circuit has held that

capital is not "costless to either the investor or the recipient"—rather, "the cost of capital is the required rate of return on various types of financing." *LaSalle Talman*, 317 F.3d at 1374–75 (quoting JAMES VAN HORNE & JOHN M. WACHOWICZ, JR., FUNDAMENTALS OF FINANCIAL MANAGEMENT 387 (10th ed.1998)). Accordingly, plaintiffs are also entitled to cost items such as the dividend and interest payments for capital-raising instruments.

The final type of reliance damage, and the one that has been in the past the most difficult to prove, is the new thrift's *costs to assume the old thrift's liabilities*. Note that this is a different theory than the liquidation cost savings restitution theory. Here, *Winstar* plaintiffs seek not to disgorge the amount that the Government allegedly saved or benefitted; rather, the reliance claim is for a cost allegedly incurred by the plaintiff upon acquiring the failing thrift.

Where plaintiffs have sought this type of damages, problems have arisen with proving the actual payment of these costs. If a profit was made or revenue was generated from the disposition of a troubled asset, then the assumption of that liability did not amount to a cost. *See CalFed*, 43 Fed.Cl. at 451–52. Often, the dollar amount claimed is for the same amount of goodwill realized in the supervisory merger.

Citing the Federal Circuit's instruction that reliance damages "provide a firmer and more rational basis" for damages, the Institutional Plaintiffs accordingly fashion their reliance claim as a cost they incurred to assume the failing thrift's liabilities, *Glendale*, 239 F.3d at 1383. However, in *Glendale*, as we noted, reliance damages were calculated by "aggregating specific costs, custodial fees, and lost historical cost of funds advantage over the bank's competitors." *Fifth Third Bank of Western Ohio v. United States*, 55 Fed.Cl. 223, 245 (2003). In fact, the Circuit has stated that damages "keyed to assumed liabilities" are "not a usable measure of

either cost to the thrift or benefit to the Government." *LaSalle Talman*, 317 F.3d at 1376-77.

We believe that damages calculated using the thrift's assumed net liabilities fail for the same reasons outlined in *Glendale*, *CalFed*, and *LaSalle*. This is especially true when plaintiffs are able to present more concrete, support reliance claims such as those discussed above.

With these general understandings in mind, we turn now to the particulars of the Plaintiffs' claims.

V. *Institutional Plaintiffs' Claims*

A. Expectation Claim for Lost Profits

The Institutional Plaintiffs seek $88.21 million in lost profits from 1990 to 1998. As discussed above, in order to prevail on its expectation claim, SoCal must prove causation, foreseeability, and reasonable certainty of damages at trial. SoCal enlisted the assistance of Dr. Paul Horvitz to prove this theory. Despite SoCal's argument that its lost profits model is both credible and conservative, we conclude that it is neither. In short, SoCal failed to prove this claim with reasonable certainty, or that its lost profits were foreseeable.

Professor Horvitz's model is based on the differences between assets of the actual bank and the projected assets of what SoCal would have had it no breach had occurred. The lost profits are calculated by applying a rate of return on the "incremental assets"—or the assets above and beyond what the breached bank actually had, Dr. Horvitz applied a 70 basis point return on the incremental assets, based upon the assumption that SoCal would have grown to $3.5 billion in assets by 1992. This $3.5 billion was projected in the original 1987 business plan.

This theory is supported by several flawed assumptions, any one of which is fatal to Dr. Horvitz's outcome. First, the reliance upon the 1987 business plan is misplaced. A plan is

merely a projection at a given point in time—it does not reveal how it is implemented; it does not account for changing or real-world market conditions; and, as the Plaintiffs acknowledge, the plan itself was ever-changing. From August 1987 to January 1989, the Plaintiffs submitted at least three other business plans. While each of those other plans may have envisioned a $3.5 billion growth target, the methods and strategies were different. Even SoCal's first president, Mr. Yunker stated "[y]ou don't look back to the business plan and simply follow it blindly. . . [i]f you were to simply write a document at a point in time and ignore what happened subsequently, you can get into a lot of trouble." Tr. 816-817. With some important exceptions, this is what Dr. Horvitz's model does.

Second, neither the business plan nor Dr. Horvitz's model accurately anticipates or deals with the California recession. The testimony indicated that the recession constrained SoCal's ability to add profitable assets. Dr. Horvitz's assumptions are based on SoCal's ability to find and capitalize on profitable assets and deposits based on a growth-through-acquisition strategy. While we are certain that SoCal would have grown more than it did without the contract capital, neither the evidence nor the testimony, nor Dr. Horvitz's model, allows the Court to know how much growth would have occurred. Further, and most importantly, growth does not necessarily equal profits.

The third error in Dr. Horvitz's model is that he fails to calculate the impact on the incremental assets of the nearly $100 million infusion of capital from the first two recapitalizations. In Dr. Horvitz's "but-for" world, SoCal would have been in a significantly weaker financial position if it had not had this additional tangible capital.

Finally, we do not believe that the central assumption in the lost profits model—the 70 basis point return on incremental assets—is credible. Upon the Court's own ques-

tioning, Dr. Horvitz admitted that the multiplier could be a bit higher or a bit lower—but that in his opinion, the 70 basis point figure was about right. Dr. Horvitz arrived at this number based on his analysis of other thrifts in the California market that actually earned a 70 basis point return, the availability of assets, and the facts specific to SoCal's financial position in the 1990's.

While the Government raised real questions about this figure when it noted that only two California thrifts achieved this level of profitability, it is absolutely wrong when it argues that SoCal "limped along" for its first two years and "never came close to earning 70 basis points." Def. Initial Br. at 3, 20. SoCal was profitable by early 1990, a condition that was only reversed when the effects of FIRREA were felt. The Government also argues that the 70 basis point figure does not include all California thrifts, only the ones that survived, and that it improperly includes thrifts of different size and condition. Dr. Horvitz's testimony was persuasive that it is appropriate to compare SoCal to these other thrifts.

Notwithstanding the flaws in the Government's defense, we remain unconvinced that Dr. Horvitz's model accurately or credibly represents SoCal's expectation damages. The assertion that 70 basis points is "modest" or "conservative" does not serve as a basis for recovery. The Federal Circuit has stated that when damages are foreseeable, a "jury verdict" approach to calculating them may be appropriate. *See Bluebonnet*, 266 F.3d at 1358. However, we do not believe that a jury verdict approach is appropriate for this claim. As Judge Hodges recently held, the Defendant "could not have foreseen at the time of contracting that plaintiff would make [certain post-breach] management decision [s]. . . ." *CalFed*, 54 Fed.Cl. 704, 713 (2002).

Here, as in *California Federal*, SoCal rightly deviated from its business plans once the breach occurred; it rightly tried new and different strategies; it replaced its executive officers;

and it did the best it could in difficult circumstances. But, as in *California Federal*, many of its actions were "independent and collateral undertakings"—and thus must be considered to be too remote and too uncertain to permit recovery. *Id.* at 713; *see also Myerle v. United States*, 33 Ct.Cl. 1, 27, 1800 WL 2024 (1897).

Accordingly, because Dr. Horvitz's theory does not satisfy this Court's standards for reasonable certainty or foreseeability, the Institutional Plaintiffs' claim for lost profits is hereby denied.

B. Restitution Claim

The Institutional Plaintiffs seek restitutionary relief in the amount of $124,573,000.00. This dollar amount represents the alleged cost savings in 1987 to the FSLIC of $348 million in avoided liquidation costs, less the $217.5 FSLIC capital credit and the $6.3 in FSLIC indemnification payments made as a part of the 1987 contract. As noted in our discussion of *Winstar* damages standards, the Federal Circuit has repeatedly rejected restitution claims based upon this calculation. *See Glendale*, 239 F.3d at 1381; *CalFed*, 245 F.3d at 1351-52; *LaSalle Talman*, 317 F.3d at 1376-1377.

As the Court stated in denying the exact theory presented by the Institutional Plaintiffs in *Fifth Third Bank*, "Federal Circuit precedent is unwavering that restitution cannot be measured" this way and the Court therefore granted summary judgment for the Defendant. 55 Fed.Cl. at 244. We agree with this reasoning, though we did permit the Plaintiffs in this case an opportunity to present evidence on this claim.

The Institutional Plaintiffs argue that their claim for restitution based upon a liquidation cost savings analysis is distinguishable from the facts in *Glendale* and *CalFed*. Those cases involved interest-rate mismatches where the acquired thrifts' insolvency was expected to resolve its problems over time, as interest rates came down. That, in fact, happened. In

contrast, we know that SoCal was a troubled institution by virtue of its stable of problem assets and other concerns, and thus they argue that time alone would not have helped the thrift or the Government. Interest rate problems aside, the Institutional Plaintiffs do not rebut another Federal Circuit point—the Government's obligation always persisted.

Finally, there is another fatal deficiency in this claim—the evidence of the quantum. The Court was persuaded by the very credible testimony of former Government analyst Kirk J. Leswing. Mr. Leswing, then an official with the FHLBB, testified at length about the Management Consignment Program (MCP) and the analytical tools used by the various divisions to evaluate problem thrifts.

Mr. Leswing's testimony illustrated vividly the problems that the Government had in analyzing and determining the extent of the financial risk each thrift posed to the insurance fund. His February 20, 1987, Memorandum entitled the "Obsolescence of FSLIC's Analytical Tools" is a case study of the problems inherent in adopting the liquidation cost analysis as a measure of restitution. *See* PX 0159. Of the model used to determine the Government's alleged liquidation cost savings, Mr. Leswing wrote:

> The model used by the Analysis and Evaluation Division (AED) was invented during the high interest rate period of the early 1980's, but its time has past, both in terms of technology and methodology. The model should not have been allowed to persist into the asset problem, stable interest period, but government being government, the model became an institution. It is absurd . . . that the model will persist . . . [t]he purpose of this memo is recommend the model be put to [an] ignominious death. . . .

Id. at 1.

Five months earlier, Mr. Leswing tried to sound the alarm bell inside the FHLBB about the failure of the FSLIC liquidation cost analysis as applied to Old Southern, in particular. Of the SoCal 1987 transaction, Mr. Leswing stated:

> The two associations with incorrect liquidation costs are [name of other thrift omitted] and Southern California S & LA, a $1.1 billion association . . . the cost [for Old Southern] has failed internal reasonability checks, but AED has not yet been consulted.

PX 0022 (Memorandum from Kirk Leswing to Mr. Robert Brick, Regional Director for Mergers and Acquisitions, Oct. 21, 1986).

We find Mr. Leswing's critiques persuasive. To address these calculation weaknesses, the SoCal Plaintiffs' expert Dr. Horvitz created a model which purports to improve the FSLIC estimate on the cost of liquidation. The Government notes in response, however, that several of the adjustments suggested by Dr. Horvitz were already accounted for, and further, that his mathematical assumptions (such as discounting on a quarterly basis instead of on a monthly basis) are incorrect. These critiques, valid though they are, go to the alleged numerical calculation of the dispute[d] benefit—they do not address more fundamental defects in the claim.

In sum, like the several judges previously faced with this theory, we are simply not convinced that this is an appropriate concept of restitution damages in this case. Whether measured as time for the Government, as the Federal Circuit has stated, or measured as a "put option" for the Plaintiffs as the Individual Plaintiffs' expert urged, the $124.5 million sought by the Institutional Plaintiffs was never paid over to the Government, and was certainly not a benefit conferred by anyone to the Government. This claim is rejected.

C. Reliance Claims

The Institutional Plaintiffs seek three forms of reliance damages—"Wounded Bank" Damages, Replacement of Lost Capital, and Assumption of Liabilities. For the reasons stated in the section on *Winstar* damages standards, we conclude that the Plaintiffs have proven their entitlement to expenses arising out SoCal's status as a wounded bank and to the costs actually incurred to replace the contract capital lost as a result of FIRREA. However, we find the claim for reliance damages based upon the assumption of Old Southern's net liabilities lacking for proof of actual payment of those liabilities.

As stated in the Factual Findings, we conclude that FIRREA harmed SoCal by removing a significant amount of contracted-for capital which was essential to SoCal's approved business plan. We further conclude that SoCal's failure to maintain capital compliance was a direct and proximate result of the Government's breach. Finally, we hold that this loss of contract capital was a substantial factor in both the increase in, or the necessity for, SoCal's actual expenses and costs from 1989 to 1996, and that these expenses were foreseeable by the Defendant.

However, we find that the effects of the Government's breach were cured by the end of 1996, the first time that SoCal both returned to profitability and earned a solid composite 3 rating. Indeed, one year after the second recapitalization, SoCal earned "3"s in each MACRO/CAMEL rating category, and it stayed above a 3 in each exam period thereafter. We accordingly limit the Institutional Plaintiffs' damages to those incurred before 1997.

1. Wounded Bank Expenses

The SoCal Plaintiffs presented uncontroverted evidence of their wounded bank expenses in the form of detailed cost notebooks complete with meticulous summaries of its bills and, and in many instances, cancelled checks. These note-

books were supported by testimony of the appropriate corporate officials. They detail increased costs in the following areas: legal, consulting and filing fees; Federal Home Loan Bank (FHLB) collateral delivery fees; excess deposit insurance premiums; and excess OTS assessments.

First, we grant SoCal's claim for legal, consulting, and filing fees in the amount of $278,258.55. *See* PX 0281 and PX 0281A (Wounded Bank Costs Notebook). Second, for FHLB Collateral delivery fees, the SoCal Plaintiffs are entitled to $64,879.42. *See* PX 0280 (Wounded Bank Costs Notbeook/Collateral Delivery Fees) (note that the Plaintiffs' claim for these costs through mid-1997 is denied). Third, to compensate SoCal for the excess in FDIC deposit insurance premiums it was forced to pay from 1989 through 1996, we award $2,509,000.00. *See* PX 0278 (SAIF Assessments Notebook) (again, denying post-1996 claims). Finally, SoCal's damages claim for the excess assessments it paid to the OTS because of its undercapitalized status is also approved, in the amount of $789,454.00. *See* PX 0279 (OTS Exam Assessments Notebook).

The total amount of damages awarded for the Institutional Plaintiffs' wounded bank expenses is $3,641,591.97.

2. Excess Cost of Funds

The SoCal Plaintiffs seek $33,900,000 in excess cost of fund damages. In determining this total amount, they offered Dr. Hartzog, a former Treasurer and CFO of the Federal Home Loan Bank of San Francisco, as their expert. His testimony, which was not persuasively contradicted by the Government's experts, was credible and thorough. Dr. Hartzog calculated SoCal's excess costs of funds using three analytical approaches. With one important adjustment, we adopt Dr. Hartzog's findings.

Dr. Hartzog analyzed SoCal's excess cost of funds using three different methods—a comparative analysis, a constant

maturity analysis, and a multiple regression analysis. We agree with Dr. Hartzog's testimony that the three analyses are mutually supportive of each other and should not be "considered in isolation . . . each [is] a part a three-part analysis that reinforce each other." Tr. 1799. Accordingly, we present each of the analyses below.

Comparative analysis

The first approach Dr. Hartzog undertook to analyze the impact of the breach on SoCal's cost of funds was a comparative analysis of SoCal's cost of funds, essentially a "before-and-after" study. *See* Tr. 1798. Dr. Hartzog compared SoCal with the 11th District Cost of Funds Index, known as COFI, which captures the total interest cost (including cost of deposits, cost of borrowing, and the cost of hedging activities) of all member institutions in the 11th District (made up of all thrifts in California, Nevada, and Arizona). The 11th District COFI is a lagging index and reflects deposits issued by 11th District thrifts over the last two prior years.

This study was designed to address whether there was indeed a widening in SoCal's cost of funds spread over COFI after the breach. Dr. Hartzog's comparative analysis showed that the spread between SoCal's cost of funds and the 11th District average widened substantially after the breach. *See* Tr. 1798-1802.

Prior to the breach, SoCal had an average 23 basis point disadvantage relative to the 11th District COFI and after the breach SoCal had an average 51 basis point disadvantage relative to 11th District COFI. *See* Tr. 1885. A comparative analysis approach similar to the one used here by Dr. Hartzog was used by the plaintiff in *Glendale* and served as the basis for Judge Smith's award of $335.4 million in excess cost of funds damages. *See Glendale*, 43 Fed.Cl. 390, 408 (1999).

In his comparative analysis, Dr. Hartzog looked at the spread between SoCal's cost of funds and the 11th District COFI, making a downward adjustment of 19 basis points to account for the exit or the resolution of weak firms by the RTC. *See* Tr. 1800. As Dr. Hartzog testified, that 19 basis point adjustment used in his comparative analysis is based on the impact reported in the well-respected article written by authors Prafulla G. Nabar and John F. Tierney. *See* Tr.1901-1902; DX 608 ("Market Dynamics of Eleventh District COFI in a Post-RTC World," JOURNAL OF FIXED INCOME, Dec. 1993, at p. 63). Dr. Hartzog's 19 basis point adjustment is consistent with his own analysis conducted during his tenure at the FHLBank—San Francisco. *See* Tr. 1887-1889.

Dr. Hartzog testified that it would not be appropriate to rely on his comparative cost of funds analysis alone to assess damages in this case, because while the comparative analysis proves that the spread between SoCal's cost of funds and that of the 11th District widened after the breach, it does not disclose what factors caused this increase. *See* Tr. 1803.

Constant Maturity Analysis

Using a second approach called a "constant maturity analysis," Dr. Hartzog determined whether on an "apples-to-apples basis," if one looked at common liability products, SoCal paid higher interest rates on the same products for which other institutions paid a lower interest rate. *See* Tr. 1798-1804. A "constant maturity analysis is used very frequently in financial markets." Tr. 1804. Dr. Hartzog's analysis looked at all of SoCal's certificate of deposits (CDs) and concluded that after accounting for the maturity differences on CDs between SoCal and the 11th District, on average, SoCal paid 41 basis points more on an equivalent maturity CD than the industry average.

Dr. Hartzog testified that it would not be appropriate to rely on his constant maturity analysis alone to assess cost of

funds damages in this case because this analysis shows SoCal paid more for its certificate of deposit (CD) products with equivalent maturities, but the analysis does not account for what factors caused this increase; moreover, it examines only CD's, one category of SoCal deposits. Tr. 1805.

Multiple Regression Analysis

Accordingly, Dr. Hartzog used a three method to calculate SoCal's excess cost of funds. This third method used a multiple regression analysis. While the Government challenged Dr. Hartzog's analysis, the Government's own expert, Dr. William Hamm, testified that multiple regression analysis has the potential to be a reliable means of analyzing economic statistics. *See* Tr. 2827. Furthermore, Dr. Hamm did not perform his own multiple regression analysis to determine the impact of capital on SoCal's cost of funds because it was not part of the "scope of [his] assignment from the Department of Justice." *See* Tr. 3341, 4817-4818. Thus, he could not rebut in any way Dr. Hartzog's findings, which we find credible and persuasive.

Dr. Hartzog's multiple regression analysis focused on the impact that capital had on SoCal's cost of funds, while taking into account other variables that were also important in affecting SoCal's cost of funds such as its profitability, growth, use of wholesale funding, and return on average assets. Dr. Hartzog determined that the loss of SoCal's regulatory capital *caused by the breach* between the period of March 1990 and December 1997 resulted in a 25 basis point (1/4 of 1%) average increase in SoCal's cost of funds relative to the 11th District COFI, resulting in $33.9 million in damages. *See* Tr. 1811-1812.

Despite the fact that interest rates did fall substantially throughout the early 1990's during the California recession, we find that this is irrelevant to SoCal's *relative* cost of funds damages calculated by Dr. Hartzog. The fact that all interest

rates went down after FIRREA does not eliminate SoCal's cost of funds damages. SoCal's Executive Vice President Doyle testified that SoCal's costs for funds were *hurt* much more than *helped* by FIRREA because despite the drop in overall rates after FIRREA, SoCal was forced to pay higher rates than its competitors which had both more capital and paid lower rates. *See* Tr. 740-742, 761. Dr. Hartzog attributed the steep decline in SoCal's absolute cost of funds after December of 1989 to the worldwide substantial reduction in interest rates. *See* Tr.1950.

Both Dr. Hartzog and Dr. Horvitz agree that it is implausible that the loss of regulatory capital had no impact on SoCal's cost of funds. *See* Tr. 1820 (Dr. Hartzog: "[i]n all my experience with financial markets worldwide, I have yet to encounter a market in which a more risky firm does not result in having higher funding costs."); Tr. 4820-21 (Dr. Horvitz: "[i]f the risk is higher, there should be some effect on return, and I don't know of [any] economists who argue that the effect is zero.").

The regulators acknowledged that weak thrifts pay more for their deposits. OTS Examiner Robert A. Baidoo, Jr., the examiner in charge of three SoCal examinations, testified that "an attribute of most of the failed institutions was that they were paying high cost of deposits because the market, that was the market." Tr. 3718. Applying that knowledge to SoCal's problems, Mr. Baidoo concluded: "[SoCal] was a failed institution, and because of that, the market basically they have to pay a—higher rates on their deposits in order to attract deposits." Tr. 3720-3721.

The Court concludes that Mr. Baidoo, and Doctors Hartzog and Horvitz are entirely accurate and credible in their analysis of SoCal's experiencing higher costs of funds after the breach. We join the Federal Circuit in concluding that the Government's breach was the substantial factor in these

increased costs. *See, e.g., Glendale*, 239 F.3d at 1383; *Bluebonnet*, 266 F.3d at 1356.

In total, the SoCal Plaintiffs seek $33.9 million in excess cost of funds damages, from the first quarter of 1990, until the last quarter of 1997. Because we conclude that the effects of the Government's breach were cured by the end of 1996, we grant damages for SoCal's excess cost of funds from the first quarter of 1990 through the last quarter of 1996, for a total amount of $32,320,000.00. For a detailed breakdown of the costs of funds by quarter, *see* PX 0347 (Calculation of Excess Cost of Funds Damages).

3. Cost of Replacement Capital/Recapitalization Costs

The SoCal Plaintiffs also presented notebooks containing the itemized bills, cancelled checks, financial statements, and other documents supporting their claim for transaction costs to replace the lost contract capital. Despite repeated attempts, the Government could not attack with any merit the costs claimed in these notebooks. Indeed, in only one instance did the Government successfully contradict any of the costs—and it was an accidental double counting that was immediately corrected.

The Federal Circuit has approved this form of reliance damages. For the reasons stated in the Factual Findings, we conclude that the Institutional Plaintiffs are entitled to these costs for the first two recapitalizations, 1992 and 1995. Costs incurred in the 1997 and 1998 transactions are hereby denied.

a. 1992 "Recap"

The SoCal Plaintiffs are entitled to $5,218,000.00 in transaction costs and expenses related to the issuance of SCH preferred and common stock and debt in 1992. We also award $556,000.00 for the payment by SoCal of dividends on the senior preferred stock issued in 1992. *See* PX 0282 (Exhibit A/Cost of 1992 Senior Notes Notebook).

b. 1995 "Recap"

The SoCal Plaintiffs are entitled to $714,374.04 in transaction costs and expenses related to the issuance of SCH preferred and common stock and debt in 1995. *See* PX 0284 (Exhibit B/Binder 2/SoCal Plaintiffs' 1995 Recapitalization Expenses). The SoCal Plaintiffs also incurred interest and dividend expenses on the stock and debt issued in 1995. Therefore, we award $3,508,000.00 in interest costs, *see* PX 0283 (Exhibit B/Binder 1/Cost of 1995 Senior Notes), and $19,439,855.40 for the payment by SoCal of the accumulated and unpaid dividends on all outstanding preferred stock issued in 1995. *See* PX 0285 (Exhibit C/Preferred Stock 1995 Cost Notebook).

c. 1997 & 1998 "Recaps"

The Institutional Plaintiff seek $17,163,000.00 in transaction costs and dividend expenses related to the 1997 REIT transaction. *See* PX 0286 (Exhibit D/1997 Preferred Stock/ REIT Notebook).

They also claim $10,593,000.00 in transaction costs and $68,753,000.00 in costs related to the redemption of preferred stock prior to the 1998 IPO. *See* PX 0287 (Exhibit E/1998 IPO Cost Notebook).

As stated above, we hold that these two transactions were undertaken for independent business purposes, wholly unrelated to the Government's breach, which we conclude was mitigated as of the end of 1996. Accordingly, we deny the Institutional Plaintiffs' claims for damages based upon expenses incurred in 1997 and 1998.

4. Assumption of Old Southern's Net Liabilities

The SoCal Plaintiffs also claim $79,188,000.00 in reliance damages for the assumption of Old Southern's net liabilities in the 1987 acquisition. This amount is calculated using the $79,660,000.00 net liability amount booked as goodwill in

1987, less an off-set for $472,000.00 in dividends paid by SoCal to SCH prior to the breach.

We do not award these damages, and for two reasons. First, as stated, we agree with Judge Miller's holding in *Fifth Third Bank* that the Federal Circuit has not endorsed this damage theory in *Winstar* cases. 55 Fed.Cl. at 245. Second, and most importantly, the Institutional Plaintiffs presented very little evidence that it actually paid down these liabilities—an absolute requirement for reliance damages. The Plaintiffs made no effort to identify the troubled loans or assets that form the basis of this claim. Though we are certain that Old Southern had a tremendous amount of liabilities which the new institution was forced to wrestle with, there was no evidence that SoCal made cash disbursements to resolve these liabilities.

Accordingly, the SoCal Plaintiffs' claim for damages based upon the assumption of liabilities is denied.

D. Conclusion to the Institutional Plaintiffs' Damages Claims

While we reject the Institutional Plaintiffs' claims for lost profits, for damages arising out of the assumption of Old Southern's net liabilities, and for the disgorgement of the alleged liquidation cost savings of the Government, we do allow, in part, their claims for wounded bank damages, for its excess cost of funds as a result of the breach, and for SoCal's actual costs of replacing the contract capital. The total amount to be awarded to the Institutional Plaintiffs is $65,397,821.41.

VI. *Discussion of Individual Plaintiffs' Claims*

A. Introduction

The Federal Home Loan Bank Board explicitly conditioned its approval of the SoCal merger transaction on the execution of the RCMA by the FSLIC, SCH, SoCal, and the Individual

Plaintiffs. Res. 87-511, p. 7, proviso 4. Thus, we held in our Liability Opinion, Secretary Simon and his fellow signatories' roles were not ancillary, as the Government urges, but rather central to this transaction. 52 Fed.Cl. at 542. The thrift would have failed—and the acquisition never have occurred —but for the Individual Plaintiffs. Our earlier recited findings make this clear beyond any peradventure of doubt.

As noted, the Individual Plaintiffs were represented by separate counsel, and advanced as their principal claims different damages theories. The expert for the Simon Plaintiffs was Dr. Allan Kleidon, a doctor in finance and economics and a corporate finance professor at the University of Chicago School of Business. The DMT Plaintiffs' expert was Dr. Roger C. Kormendi, a doctor of economics specializing in investment banking and other financial advisory services.

Prior to trial, the Individual Plaintiffs adopted each of their co-Plaintiffs' damages theories as alternative claims. During their cases-in-chief, each Plaintiff's counsel was permitted to examine the others' expert, and the Government was of course afforded an opportunity to cross examine. While we recognize that the Individual Plaintiffs have pursued different theories, we adopt one theory and use a single calculation for those damages.

The Individual Plaintiffs presented all three of the damages theories discussed above—expectation damages, restitution damages, and reliance damages. While we understand that the aim of expectation damages is to put the plaintiffs in the position they had been if the contract had been performed, for the same reasons we discussed in analyzing the SoCal Plaintiffs' claim for lost profits, it is equally impossible to do so for the Individual Plaintiffs. As to their claim for reliance damages, or the cost of performance on the contract either before or after the breach, it is also difficult to award this damage because the out-of-pocket costs caused by the breach

(i.e.: wounded bank damages and cost of replacement capital) were borne by the Institutional Plaintiffs.

The Court believes that awarding money-back restitution for their 1987 investments is not the appropriate method to value their damages or to compensate them for the harms suffered. Instead, we conclude that the dilution theory presented by Dr. Kleidon is the most accurate and credible claim advanced by the Individual Plaintiffs.

It is modeled after the Federal Circuit's holding in the *Bluebonnet* case. 266 F.3d at 1348. Because the Circuit's holding is instructive to the damages claims presented by the Individual Plaintiffs, we discuss it at some length below.

In that case, the plaintiffs, CFSB and a individual named Mr. James M. Fail, "concerned with a threat of seizure and because neither Fail nor CFSB had sufficient funds to infuse capital," borrowed money post-FIRREA from an individual to infuse capital into the thrift they had acquired from the Government in a supervisory merger several years earlier, Bluebonnet Savings Bank. *Id.* at 1352.

Several years later, by 1993, despite that first recapitalization, Bluebonnet was not generating returns sufficient to permit it to declare dividends. Like SoCal, the Government's restrictions forbade Bluebonnet from many corporate activities, such as dividends distributions, material transactions, and branch acquisitions. The dividends were necessary to allow CFSB and Fail to repay the loan. *Id.* at 1353.

Concerned with the status of the thrift, the lender/investor reached an agreement with Fail and CFSB concerning these outstanding loans called the Economic Benefits Agreement or "EBA." Under the EBA, Fail and CFSB were required to give the individual a 49% interest in the future profits of the thrift.

During their trial on damages, CFSB and Fail argued that "it would not have entered into the EBA but for the breach

and, therefore, [was] entitled to the entire cost of the EBA"—in other words, that they were entitled to the stake that they were forced to give up. *Id.* at 1356. The trial court denied that request. *Bluebonnet*, 47 Fed.Cl. 156 (2000).

On appeal, the Federal Circuit held that the plaintiffs had "persuasively argue[d]" that they would not have given up their stake in Bluebonnet absent the effects of FIRREA. 266 F.3d at 1356. The Circuit specifically noted the plaintiffs' attempts at capital raising:

> Before entering into the EBA, Bluebonnet made considerable efforts to obtain conventional financing and to acquire a . . . partner, but was unable to do so, in large part, because of the passage of FIRREA and the unfavorable climate it created for investments in thrifts.

Id.

Nevertheless, the trial court denied their claim for damages, in part because of their failure to establish a "but-for" world, which is ordinarily required to state a valid claim for expectancy damages. But the Circuit held that the trial court was "clearly erroneous." *Id.* The plaintiffs did not have to create a but-for world, presumably because the type of damages requested are not expectancy damages and because of the Court's "explicit finding" of causation.

In concluding that the plaintiffs were entitled to damages, which ultimately amounted to approximately $132 million, the Federal Circuit stated:

> In the absence of the breach, Fail and CFSB would not have agreed to the EBA because dividend financing would have been available and it would have been unnecessary to give up a significant equity stake in CFSB to obtain financing.

Id.

It is against this backdrop that we analyze the damages claims presented by the Individual Plaintiffs. As contract parties, the Individual Plaintiffs are entitled to damages from the Government's breach. As stated in the Factual Findings, we conclude that each of the Individual Plaintiffs were harmed and that the harm was separate and distinct from that suffered by the Institutional Plaintiffs. See *Strougo*, 282 F.3d at 172-75 (recognizing that forced recapitalization and "reallocation of equity" is a harm suffered by existing shareholders, and an award solely to the corporation will not compensate the equity holders for that loss).

This conclusion, that the investors were harmed individually, is supported by an earlier decision the Federal Circuit concerning the 1987 contract upon which the Plaintiffs in this case are claiming damages. As noted, the Ariadne Group brought its own separate lawsuit to vindicate its rights under the 1987 acquisition agreement. That suit was ultimately dismissed on statute of limitations grounds.

In upholding Ariadne's dismissal, the Federal Circuit stated:

> [A]s the predominant holder of preferred shares in both SoCal and the holding company that owner SoCal, Ariadne also was damaged by the government's breach. *Loss of the supervisory goodwill made SoCal, and Ariadne's investment in SoCal, considerably less valuable.*

Ariadne, 133 F.3d at 878 (1998) (emphasis added).

We also find that the Government's breach was a substantial factor in the harm suffered, the complete loss of their ownership interest. To paraphrase the Federal Circuit, in the absence of the breach, Arbur and Messrs. Doumani, Martin, Simon, and Thrall would have never agreed to the recapitalization transactions that eliminated their ownership interests. Indeed, in the absence of the breach, SoCal would

not have needed to recapitalize, and further, the Individual Plaintiffs would have continued to own their shares well beyond 1995.

Finally, we hold that it was foreseeable to the Government that new capital contributions to recapitalize SoCal after the Government's breach would result in dilution and eventual extinguishment of the Individual Plaintiffs' ownership interest in SCH common equity. *See, e.g.*, Tr. at 4175 (Mr. Shand testifies that recapitalizations involving equity can be dilutive to existing equity holders, and that such costs would be borne by the existing equity holders).

With these findings, we turn to the particulars of their alternative theories.

B. Dilution Theory

The Individual Plaintiffs dilution theory seeks to return to them their 1987 equity share that was diluted in 1992 and lost in 1995. In other words, the damages awarded under this theory either return to them the value of the breached thrift at a given point in time, or it returns to them a dollar amount of what it would cost to replace their equity in the breached thrift. *See* Tr. at 1971 (Dr. Kleidon).

Consequently, it does not seek to award damages based on what might have been if there had been no breach—in other words, as in *Bluebonnet*, no "but-for" world is required. As it is not an expectation damage theory, it does not calculate the value of the Individual Plaintiffs' share of SoCal in a non-breach world. Dr. Kleidon also does not calculate or award any lost profits or share of lost profits to the thrift caused by the breach. It merely returns to the Individual Plaintiffs their share in the breached thrift; it does not address or seek to address any increased value the thrift might have had.

This measurement of damages is based on the real world, not a hypothetical world. *See* Tr. at 2005-2007 (Dr. Kleidon explains how his calculation accounts for the competitive

conditions, interest rate environment, regulatory scrutiny, and overarching industry conditions by measuring the lost value in the actual SoCal, as it existed in the real world). To do so, Dr. Kleidon traces the SCH common equity through time—at five key stages: the initial 1987 equity; the two recapitalizations; the 1998 IPO; and the 2001 FBOP merger.

As to what assumptions his theory makes, Dr. Kleidon testified that:

> [t]here's really only one key assumption [underlying my analysis], that is that, absent the breach, SCH would not have undertaken the highly dilutive recapitalizations that it did undertake in 1992 and 1995. And what that means is that, absent the breach, the [Individual] Plaintiffs would not have had their original 1987 common equity stake cancelled without compensation by SCH.

Tr. at 1995.

When asked whether performance of SoCal in his calculation resembled its performance in the real world, Dr. Kleidon stated: "I wouldn't say it's somewhat like [the real world]. It is exactly what happened in the real world because that's what I'm basing my calculation on." Tr. at 2007. We agree with that conclusion.

We find Dr. Kleidon's method of calculating dilution damages very credible. It is simple and straightforward. He uses two methods for calculating the cost of restoration—first, by tracing the "common equity" and second, by tracing the "total equity."

The evidence indicates that the common equity method is the preferred method, and it is the one that Dr. Kleidon recommends the Court adopt. *See* Tr. at 2023. However, because the Individual Plaintiffs owned less total equity in all of SoCal in 1987 than they did common equity, the Government criticized the common equity method. Using the

total equity method—which is not "as direct [or] as straightforward as the common equity approach—Dr. Kleidon calculated the Individual Plaintiffs' lost interest as much higher than that under the common equity method." *Id.* This is because of the large conversion factors for the preferred stock into common stock during the 1998 IPO.

In other words, the total equity method overstates the harm suffered by the Individual Plaintiffs. We are persuaded by Dr. Kleidon that the common equity tracing approach is the proper method, and we adopt it here.

Using either approach, Dr. Kleidon traces what happens to the common shares acquired by the Individual Plaintiffs in 1987. At that time, they owned 100% of the SCH common stock. *See* PX 1201 (Common Stock Investors in SCH, April 30, 1987). By 1992, after the first recapitalization, their stock was converted to Class B Common, and it amounted, in total, to only 51.36% of the total SCH common stock. See PX 1202 (Common Stock Investors In SCH Following 1992 Recapitalization). By 1995, the Individual Plaintiffs owned zero shares in SCH. Their entire 100% ownership share had been eliminated without consideration during the 1995 recapitalization. See PX 1203A (Common Stock Investors in SCH Following 1995 Recapitalization).

Next, Dr. Kleidon accounts for any cash paid for common equity in either of the recapitalizations. Of the original contract signatories, only Arbur participated in 1992, paying $777 for a few shares of common equity as a part of the purchase of SoCal debt. Finding that to be "effectively zero" and statistically insignificant given the total number of outstanding shares, Dr. Kleidon rounds that number to zero. Tr. 2014.

Next, and most importantly, to account for the new equity that was issued in the 1998 public offering, Dr. Kleidon adjusts the number of shares outstanding in SCH. Pre–IPO,

the percentage of common stock was 100%. However, there is a large amount of new common stock created in the IPO, from both the conversion of the preferred stock into common, and the issuance of new shares. The net result is that the 100% common equity owned by the Individual Plaintiffs in 1987 was now only 14.41% of the SCH common equity post-IPO.

In other words, 14.41% represents the Individual Plaintiffs' post-recapitalization ownership share considered together. *See* Tr. 2020. To return the Individual Plaintiffs their interest, Dr. Kleidon then needed to determine each Individual Plaintiff's original share as a percentage of the new post-IPO common equity.

Because the Simon Plaintiffs owned 29.74% of the 1987 common stock, if they had continued to own their shares post 1998, they would have owned 4.29% (which is 29% of 14.41%), or 937,537 shares, of the breached bank. *See* Tr. 2020. Similarly, Messr. Doumani and Thrall would have 2.21% of the post–1998 thrift, and Mr. Martin would have owned 1.11%. Though Dr. Kleidon performed these calculations in Court, they are simple mathematics, not complicated financial modeling.

The final input into this equation is what market value is each share worth. Dr. Kleidon offered two possible points in time: 1998 and 2001. The importance of a publicly-traded market value for the shares of SCH common stock cannot be overstated. Not only does it permit the Court to award damages based on a concrete, non-hypothetical model, but it "provides an objective measure of the value of that equity." Tr. 1997 (Dr. Kleidon). Moreover, it gives an "objective measure of what it would cost to repurchase and replace that equity"—the central purpose behind this damages theory. *Id.*

One of the Government's testifying experts, professor of finance Dr. Allan C. Shapiro, agreed that a publicly traded

market price was the best indicator of value. *See* Tr. at 4570 (testifying that "what I would agree is that if you're trying to measure value at a given point in time, you are better off using a market value, based on a publicly traded price, than you would be if you attempted to do your own analysis, as of that specific date.").

In 1998, the price for stock sold into the public markets during the IPO was $13.75 per share. In 2001, the negotiated price for the FBOP merger was $10.00 per share.

For several reasons, the Court concludes that the 1998 date is the best date upon which to calculate damages. First, it is closer in time to the breach. We cannot be certain how long the Individual Plaintiffs might have owned their shares. The only thing of which we are certain is that they would not have walked away from their ownership interest in 1995. The testimony of each of the Individual Plaintiffs and the weight of the documentary evidence supports the conclusion that these individuals wanted to own and run SoCal. They wanted it to thrive, and made every effort to insure its eventual success. However, it is conceivable that they would have sold their shares, as the post-1995 common stock holders did, during the 1998 IPO.

Second, the 1998 market value is a more accurate value than that arrived at in the 2001 merger negotiations. It is a solid, market-driven—and market-tested, we might add—valuation. The Government's principal expert in this and in many other *Winstar*-related cases, Dr. William Hamm, testified that in his own expert report on SoCal, he used the IPO date to calculate possible damages to the Plaintiffs. *See* Tr. 3427. The Government's accountant, Mr. Randlett did so as well. *See* Tr. 3886.

We are thus convinced that Dr. Kleidon's calculation of restoring the Individual Plaintiffs' their ownership interest in the breached bank is the appropriate method of damages in

this case, and find that they should be restored their shares as of 1998. Applying the 1998 IPO price, the Simon Plaintiffs are awarded dilution damages in the amount of $12,891,113.75, or 937,537 shares times $13.75. *See* Tr. 2186 (Dr. Kleidon). Analyzed individually, the Estate of William E. Simon, Sr. is entitled to $8,624,168.00 and Arbur is entitled to damages in the amount of $4,266.965.00.

Upon questioning by counsel for the DMT Plaintiffs, Dr. Kleidon also stated that based upon that Simon Plaintiffs' damages amount, another way to examine this claim is to take the damages and divide it by the number of original shares in 1987. In doing so, Dr. Kleidon has calculated that the dilution damages as of 1998 per each share received in 1987 is $444.52 ($12,891,113.75 divided by the Simons' 29,000 shares in 1987). *See* Tr. 2043–2048; *see also* DX 0877 (Expert Report of Dr. Kleidon). Using that calculation, Mr. Doumani is awarded $6,223,280.00 in dilution damages based on his 14,000 shares. Similarly, Mrs. Thrall, as Executor of the Estate of Mr. Thrall is entitled to $6,223,280.00 (also 14,000 shares) and Mr. Martin is awarded damages in the amount of $3,333,900.00 (7,5000 shares).

The Individual Plaintiffs proved their dilution damages with more than reasonable certainty—Dr. Kleidon's calculations allow the Court to award damages based on a set point in time, using a fixed number of shares representing each Plaintiff's original ownership interest, and a real, non-hypothetical market valuation.

C. Additional Claims

1. Lost–Value Theory

The Individual Plaintiffs assert that the Government's breach caused an immediate and precipitous devaluation of their contracted-for-business opportunity, thereby allowing them to claim damages for lost-value, an expectancy theory. The DMT Plaintiffs' expert, Dr. Roger Kormendi, measured

the Individual Plaintiff's lost-value damages. Applying the "loss of chance doctrine" to measure damages for breach of contract entails determining the likelihood that performance would have benefitted the plaintiffs by a particular amount, and then "discount[ing] [the amount] to reflect this likelihood." *Koby v. United States*, 53 Fed.Cl. 493 (2002) (citing Restatement (Second) of Contracts § 348(b)).

Using a Multipath Simulation ("MPS") analysis, also known as the "Monte Carlo Model" (an unfortunate term that was not completely explained at trial), a technique for valuing financial opportunities with option characteristics, Dr. Kormendi looked forward from the time of the breach. He quantified the difference in value between the opportunity to own SoCal with almost $300 million in contracted-for regulatory capital and the opportunity to own SoCal without that capital. The DMT Plaintiffs argue that, by measuring the dramatic decline in the value of the implied option, Dr. Kormendi's MPS model appropriately measures the DMT Plaintiffs' damages here.

Dr. Kormendi also presented two separate implementations of his lost-value model. In the first, he applied the conservative assumption that the Individual Plaintiffs would not use the excess regulatory capital granted by the contract to support growth, but would instead hold it as a large capital cushion. Under this theory, the DMT Plaintiffs claim $7.84 million for Mr. Doumani and Mrs. Thrall, and $4.20 million for Mr. Martin. The Simon Plaintiffs claim $16.24 million. In the second analysis, Dr. Kormendi applied the more realistic assumption that SoCal would use the regulatory capital to support moderate growth. Under this theory, the damages claimed are $15.03 million for Mr. Doumani and Mrs. Thrall, and $8.05 million for Mr. Martin. The Simon Plaintiffs claim $31.13 million.

According to Dr. Kormendi's simulated performance paths, had there been no breach, the thrift's financial performance

could have followed any one of an infinite number of paths, with each path representing one possible course of financial performance, as measured by the level of the thrift's book equity. Some paths show immediate success; some show periods of struggle followed by success; and some show failure. Incorporating reasonable parameters to reflect actual conditions and reasonable expectations as they existed in 1989, Dr. Kormendi's model generated several thousand such paths.

All paths begin at zero tangible equity, reflecting the actual condition of the thrift at the time of the breach. In the model, the paths continue over a ten-year time horizon, with results based primarily upon: (1) long-run expected returns; (2) expectations that the thrift crisis would impair performance but that surviving thrifts would achieve higher returns after resolution; (3) reasonable leverage of surplus capital (in the moderate-growth model only); and (4) randomized variation based on the actual volatility of thrift earnings in southern California around the time of the breach. When a path in Dr. Kormendi's model takes the thrift out of regulatory capital compliance, the path hits the "line of death" and terminates with no return to the investors.

Ultimately, Dr. Kormendi determined that the breach deprived the individual Plaintiffs of a one-in-three chance of gaining $300 million in book value. Multiplying the probability that SoCal would have followed a Promise-Supported Path times the expected outcome of being on such a path determines the total harm caused by the breach in terms of book value (i.e. 1/3 H $300 million, or $100 million). Because the model simulates the thrift's performance in terms of book equity, Dr. Kormendi applied a book-to-market multiplier to convert the book-value harm into market value damages for all of the thrift's owners. Dr. Kormendi then allocated the market value damages between the common and preferred shareholders, and finally among the common shareholders, based on the shares as outlined in the 1987 contract.

As an initial matter, the Government argues that the Monte Carlo Model fails the standards for scientific reliability and acceptability. Before trial, we denied the Defendant's motion *in limine* on this same basis, and we allowed Dr. Kormendi to testify. Dr. Kormendi has excellent credentials and has worked on these issues and analyzed the S & L industry for years, among other things as a consultant to the U.S. Senate Banking Committee. Nonetheless, while we believe his model may be scientifically acceptable, we did not find that it credibly or accurately described the harm to the Individual Plaintiffs. Further, we believe the theory presented by Dr. Kormendi fails the "reasonable certainty" test as well—the very fact that it is so dependent on so many variable inputs, and generates so many thousands of expectation path conclusions, indicates, in the Court's mind, its legal flaws.

Second, and we think correctly, the Government argues that the evidence at trial refuted the DMT Plaintiffs' argument that the regulators gave SoCal an "option" to leverage the firm to incredibly low amounts of negative tangible equity. Indeed, the Government notes that the model is based upon a theory that the Plaintiffs could operate SoCal with guaranteed deposit insurance but without regulatory intervention, and continue leveraging the contract capital until the thrift had approximately $200 million in negative equity. This is a highly implausible premise—and one refuted by the contract itself. The Government correctly argues that the contract explicitly insured against the risk of "moral hazard" by including the safety and soundness provisions in the 1987 contract. Thus, the Individual Plaintiffs have also failed to prove that the Government could have foreseen the damages described by Dr. Kormendi's model.

The Defendant further asserts that the return on assets (ROA) and return on equity (ROE) parameters in Dr. Kormendi's model are improper and highly speculative, as they are based upon his own subjective beliefs regarding what

could be expected looking forward from 1989. Specifically, the Defendant points out that the model assumes that poor performance in the early years leads to higher returns in later years, even though the Government's experts testified that the opposite effect would be true.

Further, the Defendant argues that Dr. Kormendi's model unreasonably suggests that the market would have valued SoCal in 1989—now a troubled, privately-held thrift—at two-to-three times its book value, when it valued other thrifts at just 0.6 of their stated book value. Finally, the Defendant demonstrated that the model's chosen discount rate is untenable because: (1) the dramatic swings in estimates resulting from small changes in the discount rate show the unreliable and uncertain nature of the model; (2) the 10% discount rate used is dramatically inconsistent with the 20% discount rate used on preferred stock in Dr. Kormendi's replacement model; and (3) Dr. Kormendi's use of his own "hand calibrated" and result-driven 10% risk-adjusted rate flatly refutes his claim that a risk-free rate (i.e. 6%) is applicable to multipath simulations. The use of a risk-free rate is not appropriate for multipath simulation unless the risk-neutral probability distributions are applied; they are not in Dr. Kormendi's model.

In the final analysis, what Dr. Kormendi's simulation attempts to model are the DMT Plaintiffs' dimunition—or lost value—damages. For many of the same reasons that we believed that the Institutional Plaintiffs' expectation damages were flawed, we also agree with the Defendant that this Monte Carlo or MPS theory of damages is flawed. There was absolutely no proof that the Government could have foreseen the growth multiples upon which this theory is premised. Because it is too speculative, and because we cannot be reasonably certain of its application, inputs, or outcomes, we decline to adopt it here.

2. Cost of Replacement Capital Model

The Individual Plaintiffs put forward a theory on the cost of replacement capital which they argue provides an alternative measure of damages that satisfies all legal standards. Dr. Kormendi's model measured the cost the Individual Plaintiffs would have incurred had they been able to replace the contracted-for regulatory capital without dilution. In formulating the model, Dr. Kormendi modeled a hypothetical capital instrument, that is, a self-redeeming preferred stock carrying the 20% dividend rate the market required (and which would thereby qualify as regulatory capital and would amortize over the same period as the contract capital). The instrument therefore replicated the salient characteristics of the contracted-for forbearance capital that was lost as a result of the passage of FIRREA. While at trial Dr. Kormendi presented cost of replacement capital damages calculated using both the 20% dividend rate and a risk-free discount rate, in the DMT Plaintiffs' Initial Post–Trial Brief, the Plaintiffs notified the Court that they do not seek damages discounted at the risk-free rate. *See* DMT Plaintiffs' Initial Post–Trial Br. at 33.

Dr. Kormendi's model calculated cost of replacement capital without dilution damages in the amount of $15.42 million for Mr. Doumani and Mrs. Thrall, $8.26 million for Mr. Martin, and $31.9 million for the Simon Plaintiffs.

However, the Defendant criticizes Dr. Kormendi's calculations as hypothetical because the model seeks to determine the cost of replacing the contract capital without diluting the Individual Plaintiffs' contracted-for ownership interest; in other words, it seeks to determine an amount of damages on a cost that these Plaintiffs did not incur. The Defendant notes that, in asserting that the model appropriately measures the cost of cover, the DMT Plaintiffs rely upon *LaSalle Talman Bank, F.S.B. v. United States*, 45 Fed.Cl. 64, 103 (1999). However, in *LaSalle* the Court rejected the same method-

ology offered by Dr. Kormendi precisely because it was hypothetical and, therefore, irrelevant to how plaintiffs actually mitigated. *Id.*

Simply put, we do not believe that Dr. Kormendi's hypothetical model accurately reflects the damages incurred by the Individual Plaintiffs. While we believe that the breach harmed them to be sure, and while we know that they bore many costs to replace the contract capital, this damages theory is not the appropriate method to compensate them for their losses. We believe the dilution damages approach more accurately determines the loss they suffered.

3. DMT Plaintiffs' Derivative Claims

In the alternative, the DMT Plaintiffs seek three additional categories of damages. First, they seek their proportional share of any lost profits recovery that SoCal may have received. Second, they also seek their share of any recovery from either of the Institutional Plaintiffs' liquidation cost savings claim or benefit conferred restitutionary theory.

Because the Institutional Plaintiffs did not prevail on those theories, we need not address these damages claims. While we decline to reach the same legal conclusion reached by this Court in *LaVan v. United States*, 56 Fed.Cl. 580 (2003), denying derivative claims filed by investor Plaintiffs, we do not believe that these are appropriate categories of damages for these Individual Plaintiffs.

D. Money–Back Restitution

Finally, the Individual Plaintiffs claim in the alternative that they are entitled to money-back restitution. They cite the Supreme Court's decision in *Mobil Oil*, where it stated: "if the Government [breaks] an important contractual promise . . . the Government must give the [plaintiffs] their money back." 530 U.S. at 608. This principle has been applied in

Winstar-related cases. *See, e.g., Hansen Bancorp,* 53 Fed.Cl. at 98, 110.

If we did not award damages based on their dilution theory, the Individual Plaintiffs would have been entitled to money-back restitution in the amounts of money they contributed pursuant to the 1987 contract. The Simon Plaintiffs contributed $1,516,923.00; Messrs. Thrall and Doumani each invested $732,308.00; and Mr. Martin invested $392,308.00.

We do not grant these amounts in restitution because it would overlap the damages awarded under the dilution theory.

E. Government's Defenses to Individual Plaintiffs' Claims

1. No Offsets Required

The Defendant has asserted that the Individual Plaintiffs are not entitled to the return of their investment because Ariadne later cancelled the loans that financed the investment, and because SoCal Holdings paid a dividend in 1988. The Government has the burden of proving offsets, and it has not proven that any offset is appropriate in this case. *See Minnesota Chippewa Tribe v. United States,* 14 Cl.Ct. 116, 122 (1987); *G & R Corp. v. Am. Sec. & Trust Co.,* 523 F.2d 1164, 1176 (D.C.Cir.1975).

Ariadne cancelled the notes as one element of a broader global settlement with the Individual Plaintiffs. Defendant has come forth with no evidence that the Individual Plaintiffs received any net benefit from that transaction, let alone a net benefit equal to the face amount of the loans. Our holding on the Government's "Ariadne Defense" is identical to that of Judge Emily C. Hewitt in *Westfed Holdings,* another thrift that Secretary Simon's investment group rescued. 55 Fed.Cl. at 559. At trial, we received testimony about the Individual Plaintiffs' involvement in several thrifts, and about the broad nature of the Ariadne settlement. Judge Hewitt found that no

offset was appropriate in that case, holding that the settlement was "unrelated to the contract [at issue in the case]" and that it was in exchange for a "release" of a claim in "separate transaction." *Id.* We agree, and thus deny the Government's request for an offset based upon this theory.

The Government's argument that the Simon Plaintiffs' damages should be offset because of the proceeds it received from sales in 1998 and 2001, directly traceable to their investments in the two recapitalizations, is clearly wrong. The gain—if there was one—was on new money, having nothing to do whatsoever with their rights under the 1987 contract. It is as though they made money investing on widget futures, and no offset or any other reduction in damages is appropriate.

Similarly, the Defendant is entitled to no offset for any dividends declared by the thrift or holding company. Although the funds nominally passed through the Individual Plaintiffs, the investors received no net benefits from these payments, because amounts equal to the dividends were paid over to Ariadne as interest when that note was still valid.

Moreover, even if either event had benefitted the investors, the Government was not the source of the purported benefits. Accordingly, as a matter of law, the Government may not now claim these collateral "benefits" as an offset. *See Landmark Land Co. v. United States*, 256 F.3d 1365, 1374 (Fed.Cir.2001) (Government not entitled to offset where it was "not responsible" for the alleged benefit); *see also Hansen Bancorp*, 53 Fed.Cl. at 107–08 (citing *Landmark* and holding that "no offset was required because the Government was not responsible for paying the dividend [that the Government sought to offset]").

2. Plaintiffs Did Not Bear the Burden of Mitigation

Throughout the trial, the Defendant urged the Court to deny the damages claims of the Individual Plaintiffs, asserting that

they failed to mitigate the harm caused FIRREA. However, this misstates the law in a fundamental way. The Defendant, not the Plaintiffs, was obliged to mitigate damages.

> Where both the plaintiff and the defendant have equal opportunity to reduce the damages by the same act or expenditure, and it is equally reasonable to expect the defendant to minimize damages, the defendant will not be heard to say that the plaintiff should have minimized, and the plaintiff's award will not be reduced on account of damages the defendant could have avoided as easily as plaintiff.

DAN B. DOBBS, HANDBOOK ON THE LAW OF REMEDIES § 3.7 (1973); *see also S.J. Groves & Sons Co. v. Warner Co.*, 576 F.2d 524, 530 (3d Cir.1978).

In this case, "[T]he doctrine of avoidable consequences strongly argues that the government was in the best position to solve this problem." *Northeastern Pa. Shippers Coop. Ass'n., Inc. v. United States*, 32 Fed.Cl. 72, 78 (1994). Indeed, the rules of mitigation do not require the non-breaching party to subject itself to the risk of additional losses. *See, e.g., Fisher v. First Stamford Bank & Trust*, 751 F.2d 519, 524 (2d Cir.1984). This is especially true in the context of a highly fluid, unpredictable business sector such as the savings and loan/banking industry in the midst of a crisis and revolutionary new Federal regulations.

A party seeking recovery for damages due to a breach is subject to the requirement that they have not acted unreasonably so as to increase the damages which would otherwise exist. *See* 22 Am.Jur.2d Damages § 33. We find that the Individual Plaintiffs acted reasonably and diligently, and in accordance with their contractual duties under the RCMA, to assure that SoCal was capital compliant.

Nonetheless, the Defendant's mitigation argument provides an alternative measure of the damages to the Individual Plain-

tiffs. Upon questioning of each of the Individual Plaintiffs concerning their personal financial condition in 1992 and 1995, the Government seemed to urge upon the Court a theory that each should have invested an additional amount of money proportionate to their original investment percentage, up to the $100 million total raised in the two recapitalizations. In response, Plaintiffs' counsel helpfully elicited the testimony that the Government, in 1992 and 1995, not surprisingly did not offer the Simons $29 million, the Thralls and the Doumanis $14 million each, or the Martins $7.5 million in cash.

The Government's proposed mitigation theory does provide an interesting method for calculating the amount of money both the Institutional and Individual Plaintiffs would have needed to mitigate the effects of the Government's breach. If the Government had paid these Plaintiffs $100 million during the recapitalization phase, SoCal the thrift would have been instantly repaired, and the Individual Plaintiffs would not have had their ownership interest taken from them. Nevertheless, as this did not happen, it is not an acceptable damages method, and we decline the Individual Plaintiffs' suggestion to adopt it.

VII. *Conclusion*

SoCal is a *Winstar* success story. Not only was the Government's initial "supervisory goodwill" policy a success in this instance, but so were the efforts of those in charge of this particular thrift to satisfy the legislation reforming the industry.

As the Court learned during our extended trial, this institution, and these individuals, did not give up and walk away. Instead, with patience, time, money, and leadership, the Individual Plaintiffs and their management teams coaxed SoCal back to financial health and regulatory stability in the years following the S & L bailout. Because of these tre-

mendous efforts, the thrift eventually thrived. As noted, SoCal went public in 1998, generating significant capital, and eventually, merged with another California bank in 2001. It is now one of the largest banks in California.

In his conclusion in the Glendale case, then-Chief Judge Loren A. Smith noted the following:

> The court recognizes that damages, particularly involving a thrift that entered a 40–year contract 18 years ago, which was breached nearly ten years ago, necessarily is not going to be found with the precision that one could determine damages resulting from the breach of a smaller, more discrete contract. But this should not, and cannot, defeat plaintiff's claim for damages.
>
> Put simply, the government should not be immunized from paying contract damages because the extent of both the contract and breach, and the time that has elapsed between the breach and today, makes it more difficult to calculate or conceptualize damages. The court has thus endeavored to deal as best as it can with the problems posed by the passage of time and the magnitude and complexity of the contract and the government's breach.

Glendale, 43 Fed.Cl. at 410.

We are faced with the same situation. Like Judge Smith, we have endeavored, in this, our sixth published opinion in this case, to craft the best possible remedy to compensate these Plaintiffs for the Government's breach of its valuable promises.

We were dismayed at the Government's tactics in the liability phase. Unfortunately, the Government's litigation position did not improve during trial. Indeed, despite a clear finding of breach and obvious harm and expense to the Institutional and Individual Plaintiffs, even to the end of the trial, the Government contended that none of the Plaintiffs

were due even one penny in damages. While ordinary defendants are not obligated to offer a counter-theory of damages, we hold the Government to a higher standard. The Defendant continues to ignore the clear precedents of earlier *Winstar*-related damages cases.

Finally, we note that we have also experienced first-hand the Federal Circuit's observation that the "ascertainment of damages is not an exact science." *Bluebonnet*, 266 F.3d at 1355. We have followed their strict mandate not to preclude a damages award "where responsibility for damage is clear" because the amount cannot be quantified with "absolute exactness or mathematical precision." *Id.* Instead, we believe that the "evidence adduced [at trial was] sufficient to enable [this Court] to make a fair and reasonable approximation" of the compensation necessary to redress the harms suffered. *Id.* The Court believes that the monetary judgments entered today are fair and reasonable and utterly supported by the voluminous factual record of the case.

For the foregoing reasons, on Count 1, breach of an express contract, the Plaintiffs are entitled to recover the following amounts:

The SoCal Plaintiffs	$65,397,821.41
Roy Doumani	$6,223,280.00
Preston Martin	$3,333,900.00
The Simon Plaintiffs	$12,891,113.75
Beverly Thrall	$6,223,280.00

Additional Rulings

In order to permit a final judgment to be entered, we now address the remaining claims in the Plaintiffs' Amended Complaint. In a Joint Status Report filed July 21, 2003, the parties agreed that Counts 2, 3, and 4 of the Amended Complaint were subsumed in the Court's liability decision on Count 1 and are therefore moot. These Counts are dismissed with prejudice.

As to Count 5, the takings claim, the Government's position is that it is precluded by the Federal Circuit's ruling in *Castle v. United States*, 301 F.3d 1328 (Fed.Cir.2002), and should be dismissed for failure to state a claim upon which relief can be granted. The Plaintiffs stated that "if [they] are made whole by the Court's award of damages for breach of contract, they will move to dismiss Count 5 as moot." JSR, July 21, 2003. Because this Opinion today makes them whole, the Court hereby dismisses Count 5 as moot, and specifically declines to reach the Government's contention that the takings claim is barred by *Castle*.

Finally, as to Count 6, the due process claim, on July 21, 2003, the parties filed a Joint Notice of Dismissal with prejudice of that claim.

Accordingly, the Clerk of Court is directed to enter judgments for the Plaintiffs consistent with this Opinion, and to dismiss the remainder of the Amended Complaint with prejudice.

No later than twenty days after this Opinion is filed, the Plaintiffs shall submit to the Court a Joint Notice stating the exact entities or individuals to whom the judgments shall be paid.

The Defendant shall bear the allowable statutory costs of the trial on damages. The Plaintiffs shall file Bills of Costs with the Clerk of Court.

IT IS SO ORDERED.

APPENDIX C

UNITED STATES COURT OF FEDERAL CLAIMS

No. 93-52C

SOUTHERN CALIFORNIA FEDERAL SAVINGS & LOAN ASSOCIATION; SOCAL HOLDINGS, INC.; ARBUR, INC.; ROY DOUMANI; PRESTON MARTIN; WILLIAM E. SIMON, JR., J. PETER SIMON, GEORGE J. GILLESPIE, III, Executors of the Estate of William E. Simon; and BEVERLY W. THRALL, Successor to the Claims of Larry B. Thrall,

Plaintiffs,

v.

THE UNITED STATES OF AMERICA,

Defendant.

May 10, 2002

OPINION

BASKIR, *Chief Judge.*

This case is one of more than 120 *Winstar*-related cases arising out of the saving and loan crisis in the 1980's. The history behind the thrift industry's crisis and the subsequent measures taken by the Government to resolve it, have been extensively discussed in the original *Winstar* cases. *See United States v. Winstar Corp.*, 518 U.S. 839 (1996) (*Winstar IV*), *aff'g*, 64 F.3d 1531 (Fed.Cir.1995) (*en banc*) (*Winstar III*).

Pending before the Court are the Plaintiffs' *Winstar* "Short Form" Motion for Partial Summary Judgment and the Defendant's Cross-Motion for Partial Summary Judgment,

both filed in 1997. Despite the Government's dogged advocacy and its insistence on re-litigating issues that were conclusively addressed by Senior Judge Loren A. Smith of the Court of Federal Claims, the Court of Appeals for the Federal Circuit and the Supreme Court, the Court is unpersuaded by the Defendant's arguments and finds that the Government breached the contract it had with the Plaintiffs. Accordingly, we therefore must GRANT the Plaintiffs' Motion for Partial Summary Judgment on Count 1, breach of an express contract. We DENY the Government's cross-motion.

I. BACKGROUND

A. The Plaintiffs

This is a suit against the United States by a savings and loan association, its holding company, and the individuals who helped form both institutions. In the mid-1980's, one-hundred-year-old Southern California Savings and Loan Association (Old Southern), based in Beverly Hills, California, was suffering "serious asset problems" from "large operating losses, weak management, poor quality control and underwriting standards, and large contingent liabilities." Joint Status Report, filed Mar. 30, 2001, at p. 2. On June 7, 1985, the Federal Home Loan Bank Board (FHLBB), pursuant to its statutory authority over federally insured institutions, placed the insolvent thrift into receivership under the control of the Federal Savings and Loan Insurance Corporation (FSLIC). For the next year, as an alternative to liquidating the thrift and expending the FSLIC's limited insurance funds, the FHLBB and FSLIC solicited prospective purchasers or merger partners who might rescue the deeply troubled institution.

In response to these solicitations, the late former U.S. Treasury Secretary William E. Simon, Sr., formed a group of investors including, among others, former Federal Reserve Vice-Chairman and former FHLBB Chairman Preston Martin,

California real estate investors Roy Doumani and the late Larry B. Thrall, and Arbur, Inc., an investment company owned by Secretary Simon and his children. In late 1986, Secretary Simon's group submitted to the FSLIC a bid to acquire the thrift. The members of Secretary Simon's group are referred to collectively as the "Individual Plaintiffs."

The Individual Plaintiffs proposed to form and capitalize personally a holding company, to be named SoCal Holdings, Inc. (SCH), which would in turn purchase the failing thrift and form a new savings and loan association. Upon Government approval, the new association, named Southern California Federal Savings and Loan Association (SoCal), would acquire all of the assets and liabilities of its predecessor. The group's proposal, of course, contained a business plan which they believed would return SoCal to solvency and, eventually, profitability. Together, SoCal and its holding company are referred to as the "Institutional Plaintiffs."

The Plaintiffs initiated this lawsuit in 1993. Two years later, on August 2, 1995, the Plaintiffs filed a first amended complaint alleging that, by enacting the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA), Pub.L. No. 101-73, 103 Stat. 183, in 1989, the Government breached an express contract (Count 1), an implied-in-fact contract (Count 2), and the duty of good faith (Count 3). The Plaintiffs also seek restitution for breach of the alleged contract (Count 4), and further allege that the Government committed a taking without just compensation (Count 5) and violated the Plaintiffs' due process rights (Count 6).

Since 1995, some of the parties' names have changed. On July 1, 1997, SoCal changed its name to People's Bank of California and SoCal Holdings, Inc. to PBOC Holdings, Inc. Four years later, on November 13, 2001, People's Bank of California merged with California National Bank, with California National Bank the surviving institution. California National Bank is the successor-in-interest to SoCal and,

together with PBOC Holdings, Inc., continues to pursue the thrift's claim on behalf of the named plaintiffs, Southern California Federal Savings and Loan Association and SoCal Holdings, Inc. For ease of reference, the parties and the Court continue to refer to the Institutional Plaintiffs as SoCal and SCH.

Upon Mr. Thrall's death in 1998, Beverly W. Thrall, Mr. Thrall's wife, was substituted as a Plaintiff, pursuant to Court of Federal Claims Rule 25(a). Upon Secretary Simon's death in 2000, William E. Simon, Jr., J. Peter Simon, and George Gillespie, III, the Executors of the Estate of William E. Simon, were substituted as Plaintiffs, also pursuant to Rule 25(a).

Several participants to the 1987 transaction are not present in this case. The Ariadne Group filed its own independent complaint on these same facts. Its case was dismissed as untimely under the governing statute of limitations. 28 U.S.C. § 2501 (1994). *See Plaintiffs in Winstar-Related Cases v. United States*, 37 Fed.Cl. 174, 182-84 (1997), *aff'd, Ariadne Fin. Serv. Pty., Ltd. v. United States*, 133 F.3d 874 (Fed.Cir.1998), *cert. denied*, 525 U.S. 823 (1998). Its motion to intervene in this case was also denied. *See S. Cal. Fed. Sav. and Loan Assoc. v. United States*, 51 Fed.Cl. 114 (2001) (*Ariadne Intervention Order*). FIMA, another shareholder, apparently did not join in this complaint or file its own.

In addition, two members of Secretary Simon's original group did not join in either the 1993 complaint or the 1995 amended complaint. Mr. Craig Godsen has never sought to be a party to this lawsuit. Another signatory, former assistant Treasury Secretary Gerald Parsky, filed his own independent lawsuit related to the SoCal transaction. Mr. Parsky's complaint was also dismissed on statute of limitations grounds, as was his motion to intervene. *See S. Cal. Fed. Sav. and Loan Assoc. v. United States*, 51 Fed.Cl. 676 (2002) (*Parsky Recons. Order*); 52 Fed.Cl. 444 (2002) (*Parsky Intervention Order*).

B. The Acquisition and Conversion of SoCal

The Individual Plaintiffs' bid proposal regarding Old Southern was conditioned upon the receipt of substantial direct financial assistance from the Government and certain regulatory forbearances regarding minimum capital requirements. Capital requirements are "minimum reserves"-computed as a percentage of total liabilities-that the Government requires a savings and loan to maintain. *Winstar III*, 64 F.3d at 1535. The failure to "comply with minimum regulatory capital requirements [has] severe repercussions for a thrift." *Id.* As then-Chairman of the U.S. Securities and Exchange Commission Richard C. Breeden noted in 1991:

> Capital requirements are the most powerful source of discipline for financial institutions. When maintained at an appropriate level, capital requirements reduce the incentive to take excessive risks and provide a cushion against loss.

Richard C. Breeden, "Thumbs on the Scale: The Role That Accounting Practices Played in the Savings and Loan Crisis," 59 *Fordham L.Rev.* S71, S75 (1991), *cited with approval in Winstar IV*, 518 U.S. at 845-851.

The bid also specifically proposed that the newly formed institution would account for the transaction "under purchase accounting" and that:

> any excess of fair value of liabilities over the fair value of assets would be recorded as an intangible asset ("goodwill") which would be amortized over 25 years using the straight-line method, without adjustment for any reason.

Bid Proposal, at p. 8-9.

The purchase method of accounting is a generally accepted accounting practice (GAAP) for mergers. *See Winstar III*, 64 F.3d at 1535.

In January, 1987, the FSLIC accepted the Individual Plaintiffs' bid in principle and thereafter a series of exchanges took place to complete the deal. Although the dollar amount of the Government's direct cash contribution changed several times, the essential form of the transaction-a supervisory conversion using the purchase method of accounting and the infusion of cash from both the Government and several private parties-remained constant.

This transaction was executed on April 30, 1987, and was embodied in a series of several inter-related documents signed by various of the parties, including the FSLIC, FHLBB, SoCal, SCH, and the Individual Plaintiffs. These documents include:

(1) Assistance Agreement (AA), signed by FSLIC, SoCal, SCH;

(2) Regulatory Capital Maintenance Agreement (RCMA), signed by FSLIC, SoCal, SCH, and each Individual Plaintiff;

(3) FHLBB Resolution No. 87-511, reciting the particulars of the transaction; approving the supervisory conversion from a mutual to a stock association; approving the use of the capital credit in meeting regulatory minimum requirements; and approving the use of the purchase method of accounting with a twenty-five year amortization period;

(4) FHLBB Implementation Resolution No. 87-513, approving the FSLIC's expenditure of money to the new association; and

(5) Forbearance Letter from FHLBB to SCH (dated May 27, 1987), approving the use of the purchase method of accounting and the use of the FSLIC cash contribution towards meeting the regulatory capital requirements.

The Assistance Agreement contained the following integration clause:

> This Agreement, together with any interpretation or understanding agreed to in writing by the parties, constitutes the entire agreement between the parties and supersedes all prior agreements and understandings of the parties in connection with it, excepting only any resolutions or letters concerning the Conversion, the Acquisition or this Agreement issued by the Bank Board or the [FSLIC] in connection with the approval of the Conversion, the Acquisition, and this Agreement.

Assistance Agreement, sec. 18(a).

There is no disagreement among the parties that the documents referred to in the integration clause included, at a minimum, FHLBB Resolutions 87-511 and 87-513, and the FHLBB Forbearance Letter to SCH.

Together, these documents recited the following cash components of this complex transaction. First, the Individual Plaintiffs arranged for the infusion of approximately $40 million in private funds into SoCal and SCH. Second, after the FSLIC converted SoCal from a mutual savings and loan association to a stock savings and loan association, the new holding company purchased all of SoCal's common stock. Third, the FSLIC made a direct cash contribution to SoCal in the amount of $217.5 million, known throughout the *Winstar* litigation as the FSLIC "capital credit."

The private funds originated from a variety of sources. Two investment companies, Alapim Holdings, B.V., a Netherlands corporation (whose successors-in-interest are Ariadne Financial Services Partnership, Ltd. and Memvale Partnership, Ltd., collectively referred to as the "Ariadne Group") and FIMA Finance Management, Inc. (FIMA), purchased 100,000 shares of SoCal preferred stock for $33.3 million and 100,000 shares of SCH preferred stock for $1.7 million. The

Ariadne Group also loaned the individual members of Secretary Simon's group a total of $5.8 million. The Individual Plaintiffs then used most of those funds ($5.1 million) to capitalize the holding company. In return, the Individual Plaintiffs received differing amounts of SCH common stock.

The primary Government documents approving the merger, FHLBB Resolution 87-511 and the FHLBB Forbearance Letter, required SoCal to submit to the FSLIC professional opinion letters regarding the transaction. First, SCH and the Individual Plaintiffs, no later than thirty days after the close of the transaction, were required to submit an opinion of counsel letter stating, among other required items, that the AA and the RCMA "constitute valid and binding obligations" upon SoCal, SCH and the Individual Plaintiffs. Res. 87-511, paras. 12-13. Second, SoCal and SCH were required to submit an "analysis accompanied by a concurring opinion from independent public accountants" verifying that SoCal accounted for the transaction under GAAP, except where the FHLBB and the FSLIC granted SoCal exceptions from compliance with GAAP. Res. 87-511, p. 13; Forbearance Letter, para. 2. The parties all agree that these documents were submitted in accordance with the conditions set forth in the FHLBB Resolution and Forbearance Letter.

The transactional records also contained several crucial mutual promises running between various of the parties. First, the RCMA, which was signed by the FSLIC, SoCal, SCH, Arbur, in their corporate capacities, and Messrs. Doumani, Martin, Simon, and Thrall, in their individual capacities, contained a personal guarantee from each of the Individual Plaintiffs to infuse up to an additional five million dollars into SoCal should its capital fall below a certain level. RCMA, sec. 4.

Second, the RCMA specifically stated that SoCal could credit the $217.5 million Government capital contribution

towards its regulatory net worth account. RCMA, sec. 1; Res. 87-511, para. 21(b); Forbearance Letter, para. 2(a).

Third, as proposed, SoCal could account for the acquisition using the purchase method of accounting, which brings about the recognition of goodwill for accounting purposes. AA, sec. 13; Res. 87-511, para. 21(a); Forbearance Letter, para. 2(b). Because the FSLIC supervised all transactions at issue in these *Winstar* cases, this goodwill has become known as "supervisory goodwill." On April 30, 1987, SoCal booked approximately $79 million in supervisory goodwill.

Fourth, FHLBB approved SoCal's request that the supervisory goodwill could be amortized over twenty-five years using the straight line method. Res. 87-511, para. 21(c); Forbearance Letter, para. 2(b).

Fifth, the RCMA also contained a clause that if the regulatory capital fell below three percent of SoCal's liabilities, the FSLIC could repossess the institution. RCMA, sec. 7. This provision of the RCMA, along with the Individual Plaintiffs' personal cash guarantee, is key to understanding the deal. The Government specifically required the Individual Plaintiffs to sign and execute the RCMA before it would "provide [the] financial assistance and indemnification[s] set forth in the Assistance Agreement." RCMA, Recital "E", p. 2. The personal guarantees represented by their individual signatures provided extra security to the Government that the members of Secretary Simon's investment group would not walk away from the ailing thrift. This document imposed obligations on the private signatories for up to twelve years.

Taken together, the intangible goodwill promise and the tangible capital credit represented almost $300 million of Government assistance, direct and indirect, in exchange for the Individual Plaintiffs' time, leadership, and money in rescuing the failing thrift. The cost to the Government to liquidate the thrift and close it down was estimated at that

time at $235 million. As the Government document approving the acquisition stated, the FSLIC's expenditure of over two hundred million dollars, the use of goodwill, and "the acquisition of SoCal by SoCal Holdings . . . lessen[ed] the risk to the FSLIC." Res. 87-511, Marketing and Acquisition Finding No. 6, p. 17.

The Plaintiffs contend that all of these documents considered together constitute a "Final Contract," integrating the whole transaction, and creating mutually supporting obligations between the Government and the Plaintiffs.

C. FIRREA

FIRREA became law in 1989. Either directly or by mandatory regulations, it established strict new statutory capital standards for savings and loan associations, abolished both the FHLBB and the FSLIC, transferring their authority to the newly created Office of Thrift Supervision (OTS), and altered a number of existing regulations under which the SoCal supervisory conversion had occurred.

For the Plaintiffs, the most important provision of the new law related to the permissible regulatory treatment of supervisory goodwill and capital credit. Under FIRREA, "Congress expressly restricted the continued use of supervisory goodwill to satisfy regulatory capital requirements." *Winstar III*, 64 F.3d at 1538. FIRREA established three new minimum capital standards: "tangible" capital, "core" capital, and "risk-based" capital. 12 U.S.C. § 1464(t). After FIRREA's enactment, goodwill "could not be included at all in satisfying [the new] minimum *tangible* capital" requirements and only a certain amount of goodwill was permitted to be counted towards the new minimum core capital requirements. *Winstar III*, 64 F.3d at 1538 (emphasis added). The amount of goodwill includable in the core capital requirements was phased out entirely on December 31, 1994. *Id.* Further, the amortization

period for goodwill was limited to twenty years. 12 U.S.C. § 1464(t)(9)(B).

While FIRREA did not specifically address capital credits, the OTS, by regulation, equated capital credits with supervisory goodwill and phased out the Plaintiffs' ability to use them in the same manner. 12 C.F.R. 567.1(w); *Winstar III*, 64 F.3d at 1538. Thus, SoCal could no longer count the $217.5 million cash contribution by the United States towards minimum capital requirements.

Prior to the effective date of FIRREA, SoCal's regulatory capital, which included both the large FSLIC capital credit and the supervisory goodwill, was well in excess of the minimum requirements. After FIRREA and its regulations, however, OTS notified SoCal that it was a "troubled association" because it had a "substantial capital deficiency under the tangible capital requirements." Letter from Sidney C. Mar, OTS Supervisory Agent, to SoCal Board of Directors, dated Aug. 30, 1989. As a result of that deficiency, OTS imposed severe operating restrictions upon SoCal. Thereafter, SCH was forced to raise capital from outside investors in four separate rounds of financing in order for SoCal to remain solvent.

II. PROCEDURAL POSTURE

A. *Winstar* Trilogy

This case, along with other *Winstar* cases, was stayed for several years to allow three test cases-*Winstar Corp., et al. v. United States* (90-8C), *Glendale Federal Bank, FSB v. United States* (90-772C), and *Statesman Savings Holding Corp., et al. v. United States* (90-773C)—to complete their way through the Court of Federal Claims, the Federal Circuit and the Supreme Court. In each of these three cases, the Court of Federal Claims found that a contract existed and that the Government's enactment of FIRREA breached those contracts. *See Winstar Corp. v. United States*, 21 Cl.Ct. 112

(1990) (finding an implied-in-fact contract but requesting further briefing on contract issues) (*Winstar I*); 25 Cl.Ct. 541 (1992) (finding contract breached and entering summary judgment on liability) (*Winstar II*); *Statesman Sav. Holding Corp. and Glendale Fed. Bank v. United States*, 26 Cl.Ct. 904 (1992) (finding an express contract and granting summary judgment on liability to Statesman and Glendale) *(Statesman).*

The cases were consolidated for appellate review. After an initial split panel decision of the Federal Circuit reversed the Court of Federal Claims decisions, the Federal Circuit reconsidered the three cases *en banc* and affirmed the trial court decisions. *See Winstar III*, 64 F.3d 1531 (Fed.Cir.1995) (concurring with Judge Smith's holding in each case, holding that the parties formed an express contract and that the Government breached that contract when it enacted FIRREA).

The Supreme Court in turn affirmed the Federal Circuit in a plurality opinion. *See Winstar IV*, 518 U.S. 839 (1996). Justice Souter wrote the "Principal Opinion," and was joined by Justices Stevens, O'Connor and Breyer, who also wrote a separate concurring opinion. Justice Scalia agreed with the Principal Opinion's contract formation and breach holdings, but also wrote separately in concurrence to address his reasons for rejecting the Government's "unmistakability" and "sovereign acts" defenses. Justices Kennedy and Thomas joined Justice Scalia's concurrence. Chief Justice Rehnquist, joined by Justice Ginsburg, dissented, but focused only upon the Principal Opinion's treatment of the Government's sovereign defenses, not on the issues of contract formation and textual interpretation or breach. Thus, seven Justices concurred in the judgment affirming the Federal Circuit.

B. Case Management Process

After the Supreme Court issued its decision in July, 1996, this Court, under the leadership of then-Chief Judge Loren A.

Smith, devised a plan to handle the approximately 120 related cases. Pursuant to the Omnibus Case Management Order, filed on September 18, 1996, and two procedural orders filed on August 11, 1997, all of the cases were re-assigned to Judge Smith's docket, as *Winstar* Managing Judge, and were divided into several groups for discovery and trial scheduling purposes.

The process also established what was designed to be an expedited method for resolving liability issues. The plaintiffs in all *Winstar* cases were permitted to file "Short Form" Motions for Partial Summary Judgment addressing two key legal issues-whether there was a *Winstar*-type contract, and whether FIRREA breached that contract. The Government was given an extended period to respond-sixty days to file a response to formation and breach issues, and one hundred twenty days to raise any defenses.

Because the Government was unwilling to stipulate on the contract formation or liability questions, the Plaintiffs, through a specially created "Coordinating Committee," proposed that the Court consider several recurring issues and the Government's various defenses in one proceeding. Over the Government's objection, Judge Smith agreed and after selecting four sample cases, he ordered extensive briefing and extended oral argument on twelve issues common to the sample cases. *See California Federal Bank, FSB v. United States; Landmark Land Co. v. United States; LaSalle Talman Bank, FSB v. United States; C. Robert Suess v. United States*, 39 Fed.Cl. 753, 754-55 (1997) (*Cal Fed I*). The purpose of the "Common Issue Process" was to "*identify and resolve* issues common to many cases." *Id.* at 756 (emphasis added).

Judge Smith issued his opinion on eleven of the twelve common issues on December 22, 1997, and at the conclusion of that opinion, issued the following Show Cause Order. In it, he chastised the Government in unusually strong language

for re-litigating issues already determined on appeal, a failing we find repeated in this case as well.

CONCLUSION

Defendant's arguments on the eleven Common Issues Nos. 1-10 and 12 range from the rejected to the implausible. This is especially so since the arguments are heavily legal, and the government persists in ignoring or misrepresenting the law while failing to distinguish the cases factually. Summary judgment on these Common Issues is thus appropriately granted to Plaintiffs.

THE COURT THUS ORDERS THE FOLLOWING:

In all *Winstar*-related cases where there are pending summary judgment motions or cross-motions filed by the plaintiffs, the United States shall show cause, within 60 days, why those motions should not be granted, and liability found on all *Winstar* contract issues based upon the instant decision. In all cases where the government has a pending summary judgment motion or cross-motion the government shall show cause within 60 days, why those motions should not be denied, for the same reasons.

Following the submission of any summary judgment motion on liability in any *Winstar*-related case the United States shall have 90 days to show cause why that motion should not be granted on the same basis.

The government in responding to this order shall not raise issues that have been resolved by opinions in the original *Winstar* cases as clarified in this decision. Irrespective of ultimate attorneys fee issues in these cases, failure to follow this order will require the government to reimburse the plaintiffs for attorneys fees spent litigating issues that have already been resolved by this court, the Federal Circuit or the Supreme Court.

Id. at 779.

The Federal Circuit affirmed Judge Smith's determination of the Government's liability, but reversed and remanded for further consideration of the damages issues. *See Cal. Fed. Bank v. United States*, 245 F.3d 1342 (Fed.Cir.2001) (finding an express contract was formed, and that FIRREA breached that contract, despite the absence of a *Winstar*-type Assistance Agreement with a specific integration clause) (*Cal Fed II*), *cert. denied*, [534] U.S. [1113], 122 S.Ct. 920, 151 L.Ed.2d 884 (2002).

C. Common Issue Process and Show Cause Order

The essential purpose of the Common Issue Process and then the Show Cause Order was to force the Government to concede liability in cases where their defenses to contract formation and breach were foreclosed by binding opinions of higher courts, or to show the Court how an individual case was different from the test pattern on which liability was found.

Unfortunately, this procedure did not produce the result the Court intended. Because of the Government's objection to the Common Issue Process approach, the case that addressed the dozen Plaintiff-designated issues was not styled as were other *Winstar* proceedings—as a universal, all *Winstar*-related case proceeding. *See, e.g., Plaintiffs in Winstar-Related Cases v. United States*, 37 Fed.Cl. 174, 179 (1997) (discussing statute of limitations issues in all *Winstar* cases) and *Plaintiffs in All Winstar-Related Cases At the Court v. United States*, 44 Fed.Cl. 3 (1999) (discussing the issue of the FDIC's intervention in *Winstar* cases). Because the *Cal Fed I* decision was limited to *Cal Fed* facts, the common issue findings in the opinion were not adopted to each of the other *Winstar* cases on Judge Smith's docket. *See Cal Fed. I*, 39 Fed.Cl. at 779. By contrast, the Show Cause Order, founded on *Cal Fed* results, was specifically directed to every *Winstar* case at the Court of Federal Claims.

The Defendant filed its Response to the Show Cause Order as respects this case on February 20, 1998, and the Plaintiffs filed a Proposed Order for Partial Summary Judgment on Liability on March 31, 1998. Judge Smith did not render a decision on the Defendant's Response to the Show Cause Order in this case, nor did he act upon the Plaintiffs' Proposed Order. Once fact and expert discovery was complete in June, 2000, the Response to the Show Cause Order, along with other pending issues, was transferred to this Court in November, 2000.

The Government's Response objected to the adoption of the Show Cause process, stating that it believed that "[the Show Cause Order] unjustifiably reverses the burden of proof" in this case. Def. Resp. to Show Cause Order, filed Feb. 20, 1998, at p. 31. Accordingly, we will not issue a final ruling on Judge Smith's Show Cause Order. We will instead base our decision upon the Briefs and Oral Arguments supporting Plaintiffs' underlying motion for summary judgment and the Defendant's cross-motion.

D. Issues to be Decided

The Court must resolve three issues: First, whether the five documents we have cited constitute one contract and whether the Individual Plaintiffs were parties to this overall agreement; Second, whether the transactional documents created a contract with the Plaintiffs concerning SoCal's ability to count the $217.5 million capital credit and the $79 million in supervisory goodwill towards the thrift's regulatory capital requirements; and finally, if we determine that a contract existed with promises involving capital credits and supervisory goodwill, whether FIRREA breached that contract and those promises. Before we turn to a consideration of these questions, we will first review the legal context in which they are presented.

III. *WINSTAR* PRECEDENTS

While the undecided liability issues in this *Winstar* case are not new, they are before the undersigned judge for the first time. Accordingly, we find it helpful to set out a brief history of the *Winstar* precedents that, of course, are binding on this Court.

The parties agree that the transaction that is most like the one at issue here is the transaction that was presented in the *Statesman* case, 26 Cl.Ct. at 904. In 1988, Statesman Savings Holding Corporation (Statesman) acquired four insolvent savings and loans in a supervisory conversion. As a part of the deal, the FSLIC provided Statesman with a cash contribution—a capital credit—of $60 million. *Id.* at 907-08. Further, Statesman was permitted to account for the acquisition using the purchase method of accounting, which created approximately $25.8 million in goodwill. *Id.* Statesman was allowed to amortize the supervisory goodwill over a twenty-five year period. The terms of the agreement between Statesman and the Government were memorialized in an Assistance Agreement, with a clause integrating a Regulatory Capital Maintenance Agreement and several FHLBB resolutions and letters. *Id.*

The Court of Federal Claims held that these documents constituted one over-arching contract between the thrift, its investors, and the United States. *Id.* at 912. It further concluded that FIRREA breached the express contract the Government had with Statesman and that "the government is liable to Statesman for its decision not to honor either of these promises." *Id.* at 916. As noted, the Federal Circuit and the Supreme Court affirmed Judge Smith's contract formation and liability conclusions. *See Winstar III*, 64 F.3d at 1541-43; *Winstar IV*, 518 U.S. at 867.

In resolving the various liability issues in our case, we are guided first by the precedential force of the *Winstar* cases.

Textual interpretations of the documents in these cases would control our own interpretations of the documents in this case unless, of course, textual differences or underlying factual differences dictate a different legal conclusion. Moreover, the analyses and conclusions of our colleagues in other *Winstar* decisions offer helpful guides to our own analysis and conclusions. We do not write on a clean slate nor, to shift metaphors, are we compelled to cut a new path through an uncharted *Winstar* wilderness.

Although we are not implementing Senior Judge Smith's Show Cause procedure, and we do not shift any burdens of persuasion, as a practical matter it behooves the Government to show us how the specific facts and texts in this case are so different as to compel a different result than was reached by the Supreme Court and the Federal Circuit.

As my fellow Judge Eric G. Bruggink stated in another *Winstar* opinion on liability:

> We cannot ignore the fact that the contractual provisions we are called upon to interpret here are remarkably similar to provisions considered in *Winstar*. We are not, therefore, interpreting the words of this contract in a vacuum. Consequently, we find it useful to set out, in table format, the relevant contractual language in these transactions alongside the corresponding language in the documentation of the various transactions at issue in *Winstar*.

Home Sav. of Am. v. United States, 50 Fed.Cl. 427, 435 (2001).

We think the Judge has the right approach. We will look, therefore, for textual or factual differences, or legal issues not previously decided in determining the liability question in this case.

To aid in this analysis, we asked the parties to submit as a joint appendix those contractual documents in *Statesman* which formed the foundation for the higher court's legal conclusion. The relevant provisions from the *Statesman* documents, compared to the equivalent provisions in the SoCal documents, are contained in an Appendix to this Opinion. A careful reading of Comparison Charts I-VII reveals that the provisions in the two sets of documents are not materially different from each other in any respect. Further, it is interesting to note that the *Statesman* documents, from March 1988, are one year older than the SoCal documents, from April 1987.

IV. DISCUSSION

Pursuant to the *Winstar* case management process, Plaintiffs filed a Short Form Motion for Summary Judgment, but did not file proposed findings of fact. However, from the parties' motions, cross-motions, and briefs, it is clear that the relevant documents and facts are undisputed. Furthermore, the Government concedes that it had an express contract with the institutional Plaintiffs, SoCal and SCH, and that, at least with respect to the FSLIC capital credit, FIRREA breached that contract. What remains in dispute is whether the Individual Plaintiffs were parties to that contract, and whether the Government breached that contract with respect to supervisory goodwill. Because the relevant facts are not in dispute, the issues presented here are appropriate for summary judgment. *See Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242 (1986).

Before we turn to the merits of the Plaintiffs' motion, however, the Court must note a procedural technicality. The Short Form Motion was made only on behalf of two of the Plaintiffs, SoCal and SCH. The Individual Plaintiffs (represented by different counsel from the Institutional Plaintiffs) did not join in the motion or file their own. The Defendant's response papers, however, assume that all the Plaintiffs joined

in the motion. Indeed, in the four years since the Short Form Motion was first filed, the parties have acted as if each Plaintiff had moved for summary judgment.

This oversight was corrected at oral argument, when counsel for Plaintiffs Arbur, Inc., the Executors of Secretary Simon's estate, Mr. Doumani, and Mrs. Thrall moved the Court for permission to join in the original motion. The Government did not object and thus the Court, on November 20, 2001, deemed the Short Form Motion for Partial Summary Judgment to have been joined and filed by all the Plaintiffs.

A. Sole Benefit Clause

The first issues to be resolved are whether the five documents we have cited constitute one contract and whether the Individual Plaintiffs were parties to this overall agreement. A number of independent analyses compel us to conclude both issues in favor of the Plaintiffs.

The Assistance Agreement, to which only SoCal, SCH, and FSLIC were signatories, contains a clause which the Government argues limits the benefits of that agreement to only the Institutional Plaintiffs. The Individual Plaintiffs, meanwhile, argue that not only did they sign one of the other transaction documents, the Regulatory Capital Maintenance Agreement, but that the Assistance Agreement and the FHLBB implementing resolutions specifically required each of those other documents to be signed in order to complete the transaction. Thus, they conclude that notwithstanding the apparent limiting reach of the "sole benefit" clause, there is one contract and they are parties to it.

The Government's argument is incorrect, both as a textual matter and by precedent. First, we apply the traditional maxim that all provisions in a contract must be read so as to give meaning to each, if at all possible. *See, e.g., Brinderson-Newberg Joint Venture v. Pacific Erectors*, 971 F.2d 272 (9th

Cir.1992) ("It is a cardinal rule in interpretation of contracts that the contract is to be taken by its four corners and so construed as to give effect to every part of it, *if possible*.") (citations omitted) (emphasis added). The Government's interpretation violates this maxim, creating a conflict with another provision of the document. But Section 21, the "sole benefit" clause, Appendix Comparison III, does state that the Agreement is for the "sole benefit of the parties hereto and for the benefit of no other person." Section 18 of the Agreement, the "entire agreement" clause, Appendix Comparison II, specifically adopts each of the other documents and agreements executed contemporaneously with the Assistance Agreement as part of the overall contract between the parties, including the RCMA. In fact, the very validity of the Assistance Agreement was conditioned upon the Individual Plaintiffs' execution of the RCMA:

> The [FSLIC]'s obligations pursuant to this Agreement are also conditioned upon the following: . . . The execution and delivery by [SCH], [SoCal], and the Investors [each Individual Plaintiff and Messrs. Godsen and Parsky, but not the Ariadne Group or FIMA], as appropriate, of the Regulatory Capital Maintenance Agreement. . . .

Assistance Agreement, sec. 2(b).

The Federal Home Loan Bank Board also explicitly conditioned its approval of the transaction on the execution of the RCMA by the FSLIC, SCH, SoCal, and the Individual Plaintiffs. Res. 87-511, p. 7, proviso 4. Thus, Secretary Simon and his fellow signatories' roles were not ancillary, as the Government urges, but rather central to this transaction. The thrift would have failed—and the acquisition never have occurred—but for the Individual Plaintiffs.

Furthermore, the "entire agreement" clause also states: "If any provision of this Agreement is invalid or unenforceable,

all of the remaining provisions of this Agreement shall nevertheless remain in full force and effect. . . ." AA, sec. 18. The "sole benefit" clause, to the extent that the Government is attempting to use it to limit its liability to the Individual Plaintiffs, would be one such unenforceable provision.

We conclude that the Government, in signing the Assistance Agreement, the RCMA, and the FHLBB implementing resolutions, with all the parties on the same day, intended to contract with all the Plaintiffs—the Institutional Plaintiffs and the Individual Plaintiffs.

Our conclusion is not a new one. The integration clause at issue here is not materially different from the one in *Statesman*. In that case, Judge Smith held that that integration clause "specified the documents that would control the interpretation of the parties' agreement." *Statesman*, 26 Cl.Ct. at 908. Judge Smith concluded that those documents included the Assistance Agreement, the RCMA, the FHLBB Resolutions, and the FHLBB Forbearance Letter. *Id.* The Federal Circuit endorsed Judge Smith's finding that the integration clause "incorporated [the] contemporaneous resolutions of the Bank Board." *Winstar III*, 64 F.3d at 1543. The Principal Opinion of the Supreme Court agreed with that conclusion, stating:

> To the extent that the integration clause leaves any ambiguity, the other courts that construed the documents found that the realities of the transaction favored reading those documents as contractual commitments, not mere statements of policy . . . and we see no reason to disagree.

Winstar IV, 518 U.S. at 863.

We also see no reason to disagree.

Indeed, the Government initially acknowledged that these transactional documents created one overall contract. Their

response and cross-motion refers to the documents signed by the parties as one agreement:

> On or about April 30, 1987, SCH acquired SoCal pursuant to certain agreements by and between SCH, the [FSLIC], and the [FHLBB]. These agreements are embodied in an Assistance Agreement, Regulatory Capital Maintenance Agreement, FHLBB Resolution No. 87-511, and a FHLBB Forbearance Letter (collectively, the "Agreement").

Def. Resp., filed June 13, 1997, p. 3 (citations omitted).

In that same document, the Government, in a title to the section where it concedes breaching the capital credit promise, states:

> There is no dispute that a contract exists between Plaintiffs and the Government concerning the capital credit and that FIRREA is inconsistent with the terms of that contract.

Id. at p. 11.

In that first written response to the Plaintiffs' motion, the Government did not challenge the Individual Plaintiffs' contractual status. A month and a half later, however, in the Defendant's 120-Day Response to Plaintiff's Motion for Partial Summary Judgment, the Government did assert that the Individual Plaintiffs "may not properly assert breach of contract claims against the Government under the Assistance Agreement because plaintiffs lack privity of contract with the Government." Def. 120-Day Resp., filed Aug. 1, 1997, at p. 17. The narrow language of that standing challenge, though, is confined only to the promises contained in the Assistance Agreement. The Government never challenged the Individual Plaintiffs' standing to sue under the Regulatory Capital Maintenance Agreement, to which the FSLIC, SCH, SoCal, and the Individual Plaintiffs are all signatories.

And, as noted above, Section 1 of the RCMA contains an explicit promise that SoCal could use the FSLIC capital credit towards meeting minimum capital requirements. The Government concedes that the RCMA contained this promise. Accordingly, from the four corners of the Government's written responses, then, it appears that they have indeed conceded that a contract does exist between the Government and each of the Plaintiffs with respect to the capital credit.

At oral argument, however, counsel for the Defendant seemed to assert the exact opposite, stating:

> The shareholder Plaintiffs have continued to maintain that we conceded an issue with respect to capital credit with respect to all parties, and it's very obvious from the pleadings that we did not, that we conceded that only with respect to the thrift.

Oral Argument Tr., Nov. 20, 2001, at p. 8.

The Government argued that the "sole benefit" clause limited the contract to the Institutional Plaintiffs only, notwithstanding the Individual Plaintiffs' obvious participation in the execution of the RCMA. Essentially, it now argues that its written concession is only to some of the RCMA's signatories, not all of them. At oral argument, counsel for the Government contended that despite the fact that each Individual Plaintiff signed the RCMA in their individual capacity, because they did not also sign the AA, no contract was formed with them.

The Government's concession that an overall contract was created consisting of a number of separate instruments, cannot co-exist with its narrowly crafted challenge to the Individual Plaintiffs' standing as respects one of those instruments. The Government cannot agree that a contract exists and that FIRREA breached that contract with respect to some of the signatory parties, and at the same time deny that that same

contract exists with other of the parties in order to avoid a finding of breach with respect to those latter parties.

Moreover, the Court considers the Government's use of the "sole benefit" clause defense, and its change of position at oral argument that a previously filed, written concession was not really one after all, both to be out of order. These issues have been pending for nine years, and have generated a considerable number of substantive filings. While we recognize that current Government counsel did not represent the Defendant when the Response briefs were originally filed, the Court believes that the Department of Justice's change of position on this issue, *with no notice to the Plaintiffs or the Court*, was procedurally improper and unfair. Such "gotcha" tactics are wholly inappropriate.

Thus, the Government's argument—that this was not an integrated agreement that included the Individual Plaintiffs—is rejected. The Court finds that the Government was a party to an express contract with SoCal, SCH, and the Individual Plaintiffs. We shall refer to this agreement as the "Overall Contract."

B. Capital Credit

As we have stated, the Government concedes that the transactional documents created an express contract with SoCal concerning its ability to count the $217.5 million FSLIC capital credit towards the thrift's regulatory capital requirements, and that FIRREA breached that promise. The Defendant's capital credit concession represents a refreshing display of legal reality that has not been typical of the Department of Justice's litigation position in these *Winstar* cases since the Supreme Court issued its opinion in 1996.

Because the Court today finds that the Individual Plaintiffs were parties to the Overall Contract for SoCal's conversion, the capital credit promise runs to them as well. Thus, we must also hold that FIRREA breached the capital credit prom-

ise made to the Individual Plaintiffs. Accordingly, the Plaintiffs' motion for partial summary judgment is GRANTED as to this breach.

C. Supervisory Goodwill

The only remaining liability question before the Court is whether the Government breached the Overall Contract with respect to supervisory goodwill. The Government conceded during oral argument that the contractual language reciting the use of the purchase method of accounting and its twenty-five year amortization period constitutes a binding promise. However, the Government asserts three defenses to the breach: First, that the documents do not contain an explicit promise to count the supervisory goodwill towards regulatory capital; second, that the Plaintiffs bore the risk of change in an uncertain regulatory environment; and third, that because SoCal did not need the supervisory goodwill to keep it solvent, it was not a part of the contract. To *Winstar* cognoscenti, these arguments are *deja vu* all over again.

i. Missing Promise Theory

The Defendant's missing or second promise theory has been considered and rejected by every court that has considered it, including a majority of the Supreme Court. Undeterred, the Government raises it again here. This defense theory was foreclosed by clear precedent—precedent that was issued in 1995 and 1996. Thus, we were more than a little distressed to see the "missing promise" argument re-emerge in our case. In its 120-Day Response, filed in August of 1997, the Government raised the very same argument that a majority of the Supreme Court had plainly rejected one year earlier: "No implied contractual promise to count supervisory goodwill towards regulatory capital was created by the SoCal transaction." Def. 120-Day Resp., at p. 5. Further, at oral argument, counsel for the Defendant stated: "We never made a promise that it [supervisory goodwill] would be counted as

regulatory capital or even capital." Oral Argument Tr., at p. 36.

Whether the Department of Justice believes it or not, the Supreme Court's *Winstar* trilogy is controlling legal authority and binding upon this Court. The Government has not addressed this precedent, nor attempted to explain why it does not preclude its re-assertion in this case.

In any event, in support of this defense, the Government again points to the text of the Overall Contract and notes that the documents do not explicitly state that the thrift can use supervisory goodwill towards meeting the regulatory capital minimums.

In the first *Winstar* case, Judge Smith rejected that theory, holding instead that the documents clearly showed that the Government "expressly intended to contract for the particular treatment of goodwill at issue in this case" and that that contract allowed the thrift to count supervisory goodwill towards regulatory capital minimums. *Winstar I*, 21 Cl.Ct. at 115. The Federal Circuit concurred with Judge Smith's holding, stating:

> If the parties did not intend to use supervisory goodwill for regulatory capital purposes these would simply be no reason for the extensive negotiations and the conditions regarding its use.

Winstar III, 64 F.3d at 1542.

Not content with the rejection of their "missing promise" argument in the lower courts, the Government, upon appeal to the Supreme Court, continued to argue that because some necessary language was missing from the documents, the Government had made no such promise. In its Brief to the Supreme Court, the Government wrote:

> The contract provisions on which the Federal Circuit relied in this case do not in fact contain promises that

> respondents' goodwill will continue to be counted for purposes of satisfying federal regulatory capital requirements . . . the relevant portions of those documents [the Assistance Agreements and FHLBB resolutions and forbearance letters] contain directives as to what respondents must do to comply with current regulatory policy, not commitments by the government to continue to permit goodwill to be counted as capital.

Winstar IV, Br. for the Pet'r, 1996 WL 99716, at p. 11.

The Principal Opinion explictly rejected this argument, stating:

> The Government . . . insists . . . that these [merger] documents simply reflect statements of then-current federal regulatory policy, rather than contractual undertakings. Neither the Court of Federal Claims nor the Federal Circuit so read the record, however, and we agree with those courts that the Government's interpretation of the relevant documents is fundamentally implausible.

Winstar IV, 518 U.S. at 862.

These courts held that an explicit second promise is not necessary because of the inclusion of the specific section of the Insurance Regulations in effect at that time, § 561.13, which permitted thrifts to use any asset (tangible or intangible) in computing regulatory capital. Thus, the second promise—using goodwill towards regulatory capital—is subsumed in the first promise—using the purchase method of accounting and a longer amortization period. That same provision is present in our Overall Contract. AA, sec. 13; Res. 87-511, paras. 21(a-c); Forbearance Letter, para. 2(b). As counsel for the Institutional Plaintiffs noted at oral argument, the Government "wants two things: a belt and suspenders." As a majority of the Supreme Court has said, a second such promise (or bracing device) is not necessary to hold that a contract was formed. *See Winstar IV*, 518 U.S. at

862-63. Thus, as previous Courts have done, we too reject the Government's "missing promise" argument.

ii. Assumption of the Risk

As its second defense, the Government argues that the private parties to the contract assumed the risk of a regulatory change in the treatment of capital. Once again, the Government advances an argument explicitly considered and rejected by the appellate courts, and does so without addressing-much less distinguishing-the applicable precedent. We devote more space in rejecting it than it truly deserves.

The Government argues that Section 1 of the RCMA assigns to the Plaintiffs the risk of a change in regulatory rules governing the treatment of supervisory goodwill as capital, including the changes mandated by FIRREA. RCMA Section 1 states, essentially, that SCH and the Individual Plaintiffs shall cause SoCal's "regulatory capital" to be "maintained at the level required by § 561.13(b) of the Insurance Regulations" in effect at that time (1986) or "*any successor regulations, as now or hereafter in effect.*" RCMA, sec. 1 (emphasis added). The underscored language follows the reference to the "definition" of regulatory capital, and is repeated in the reference to the "levels" of regulatory capital which follows immediately thereafter.

The successor regulation language, presented in the Appendix at Comparison Chart IV, is the same language that was used in the *Statesman* transaction, even as to its repetitive supererogation. The Federal Circuit and the Supreme Court also considered the "assumption of the risk" argument, and, as with the "missing promise" theory, explicitly rejected it. Analyzing the agreements presented in the original Winstar transaction, the Federal Circuit noted that the Winstar, Statesman, and Glendale thrifts were—

> bound to keep in compliance with banking regulations and laws regarding capital levels except to the extent the

> Bank Board expressly agreed to forbear from enforcing its regulations against it. This stipulation by Winstar to maintain its regulatory net worth at whatever level the regulators set does not, however, eclipse the government's own promise that Winstar could count supervisory goodwill in meeting the regulatory requirements with which it had promised to comply.

Winstar III, 64 F.3d at 1544.

A majority of the Supreme Court expressly affirmed the lower courts' rulings on this subject. Indeed, in the opening paragraph of the Principal Opinion, Justice Souter stated:

> [W]e hold that the terms assigning the risk of regulatory change to the Government are enforceable, and that the Government is therefore liable in damages for breach.

Winstar IV, 518 U.S. at 843.

Further, the Principal Opinion viewed the Defendant's "assumption of the risk" theory as a corollary argument to the "missing promise" theory. Justice Souter, discussing the Statesman transaction, noted that by including in the contract a then-concrete statutory scheme, the Government was contractually bound to honor its promise to apply those same regulations:

> The Government asserts that the reference to § 561.13 of FSLIC regulations, which at the time defined regulatory capital for thrift institutions, indicates that the Government's obligations could change along with the relevant regulations. But, just as in Winstar's case, the Government would have us overlook the specific incorporation of the then-current regulations as part of the agreement. . . .

And continuing:

> It is important to be clear about what these contracts did and did not require of the Government. Nothing in the

> documentation or the circumstances of these transactions purported to bar the Government from changing the way in which it regulated the thrift industry. Rather, what the Federal Circuit said of the Glendale transaction is true of the Winstar and Statesman deals as well: "the Bank Board and the FSLIC were contractually bound to recognize the supervisory goodwill and the amortization periods reflected" in the agreements between the parties. We read this promise as the law of contracts has always treated promises to provide something beyond the promisor's absolute control, that is, as a promise to insure the promisee against loss arising from the promised condition's nonoccurrence. . . .
>
> *When the law as to capital requirements changed in the present instance, the Government was unable to perform its promise, and therefore became liable for breach.*

Id. at 868-870 (quoting *Winstar III*, 64 F.3d at 1541-42) (emphasis added).

A review of the "assumption of risk" or "successor regulation" language in Comparison Chart IV does demonstrate some minor textual differences. Section 1 of the SoCal RCMA is longer than Section 1 of Statesman's RCMA, but the meaning is unchanged, and the Government does not argue otherwise. (In August of 1986, the Federal Home Loan Bank Board amended its regulatory net worth regulations. Regulatory Capital Requirements of Insured Institutions, 51 Fed.Reg. 33,565 (Sept. 22, 1986) (to be codified at 12 C.F.R. § 561.13). The new regulations increased the level of and altered the method for calculating regulatory net worth. *Id.* Though final, the new regulations were not expected to be codified until after the SoCal transaction documents were signed. Accordingly, the language in the SoCal documents could not merely cite to the CFR version-it had instead to discuss the new regulatory scheme and cite repeatedly to it, as printed in the *Federal Register*.)

It is important to note that the Supreme Court, reviewing the *Winstar* trilogy, was presented with regulations spanning an eight year period. The Glendale transaction was completed in November 1981; Winstar was completed in July, 1984; and Statesman was completed in March 1988. Accordingly, the Supreme Court's decision is not confined to one edition of statutes or regulations, but rather holds that FIRREA breached insurance regulations spanning from 1981 to 1989. Justice Souter noted that "although substantial changes had been introduced into [the successor regulation language set forth in] § 561.13" by 1988, none of the regulations at issue "resolve the basic ambiguity as to whether goodwill could qualify as regulatory capital." *Winstar IV*, 518 U.S. at 854, n. 9. The transaction at issue here was completed in April of 1987, and thus the Principal Opinion's reasoning encompasses the version of the regulations set forth in SoCal's contract with the Government.

Finally, we must state that, as with each of the other defenses raised by the Government, other courts have discredited this theory as well. After the Supreme Court's decision in 1996, Judge Smith, relying on Justice Scalia's opinion in concurrence in *Winstar IV*, rejected the "assumption of risk" argument in *Cal Fed I*:

> If, as the dissent believes, the Government committed only "to provide [certain] treatment unless and until there is subsequent action" [*Winstar IV*, 518 U.S. at 935], then the Government in effect said "we promise to regulate in this fashion for as long as we choose to regulate in this fashion"—which is an absolutely classic description of an illusory promise.

Cal Fed I at 776-78 (citing *Winstar IV*, 518 U.S. at 921 (Scalia, J., concurring)).

The contractual language before us is no different than that which was before the Supreme Court in *Winstar*. Thus, the

Defendant's argument that the Plaintiffs bore the risk that the regulations might change must fail here as well.

iii. "Reverse Madness"

In its efforts to persuade this Court to find no contractual promise with respect to regulatory goodwill, the Government points not to the text of the integrated contract, but to an argument offered by the Principal Opinion in discussing the *Glendale* case, one of the *Winstar* trilogy. In *Glendale*, the new, merged thrift's financial situation was such that absent the goodwill, it would have failed and been subject to penalties "from the moment of its creation." *Winstar III*, 64 F.3d at 1542. In that transaction, the supervisory goodwill was needed from *day one* as an initial remedial component just to bring the thrift into compliance with the capital regulations.

A majority of the Supreme Court pointed to this necessity as part of the evidence that the parties intended that the supervisory goodwill would count towards regulatory capital. The Principal Opinion said:

> [I]t would have been irrational in this case for Glendale to stake its very existence upon continuation of current policies without seeking to embody those policies in some sort of contractual commitment. This conclusion is obvious from both the dollar amounts at stake and the regulators' proven propensity to make changes in the relevant requirements. . . . Under the circumstances, we have no doubt that the parties intended to settle regulatory treatment of these transactions as a condition of their agreement.

Winstar IV, 518 U.S. at 863-64 (citations omitted).

Justice Souter concluded his opinion by noting:

> *It would, indeed, have been madness* for respondents [Winstar, Glendale, Statesman] to have engaged in these transactions with no more protection that the Govern-

> ment's reading would have given them, for the very existence of their institutions would have been in jeopardy from the moment their agreements were signed.

Id. at 910 (emphasis added).

By contrast, the Government points out that while SoCal was ailing, it was not in as bad a condition as the thrift was in *Glendale*. Thus, while the approximately $79 million in supervisory goodwill was helpful in shoring up SoCal's financial statement, it wasn't essential to meet regulatory minimums. As a consequence, the Defendant now argues a "reverse madness" theory; namely, that because it would *not* "have been madness" to enter into this transaction without a binding supervisory goodwill promise, there must have been no promise at all.

As with its first two defenses, the Defendant raises another discredited argument. In addressing the common issues in *Cal Fed I*, Judge Smith discussed the Government's "reverse madness" theory:

> The government's position can be summed up as arguing that if a deal was not insane absent a contractual commitment, then there is no contract. *Seldom has a court heard such a bizarre method of determining contractual intent.* When this proposition is put forth by the United States of America one is almost tempted to wonder if insanity is indeed a prerequisite for contracting with the government.
>
> . . .
>
> The government takes one piece of the evidence of contractual intent found by the Supreme Court, the Federal Circuit, and this court, and turns that one piece of evidence of intent into a litmus test for when a contract exists in all cases. *This is a rendering of the court's decisions that literally turns them on their heads.*

Cal Fed. I, 39 Fed.Cl. at 767-68 (emphasis added).

As we note above in Section II, Judge Smith's common issue holdings were not adopted to the remainder of the *Winstar* cases on his docket. Furthermore, we recognize that this latest defense theory has not yet been officially rejected by the appellate courts. This is faint support, indeed.

We are not persuaded for a number of reasons. First, the Supreme Court did not hold that the promise could only exist if the thrift would otherwise have failed at the start. It simply observed that the fact that the thrift would have failed without the inclusion of the supervisory goodwill supported a reading that the parties' clearly intended to contract for that particular promise. The Government offers no authority for treating this factor as a *sine quo non* of the contract.

Second, the parties in both transactions were endeavoring to save a troubled thrift, and were negotiating to put the institution in as strong a position as circumstances permitted. Under these facts, the agreements which comprise the Overall Contract, with the inclusion of the promise to allow the $79 million in supervisory goodwill to count towards regulatory capital, put the new thrift in a regulatory capital position almost one-third greater ($79 million out of a total of $297 million) than it would have been without the goodwill.

The amount of regulatory capital represents more than a "go-no go" regulatory threshold for a thrift. The amount of capital determines how much is available for loans by the institution, the essence of its money-making operation. As the Principal Opinion observed, treating supervisory goodwill and capital credits "as regulatory capital was attractive because it inflated the institution's reserves, thereby allowing the thrift to leverage more loans (and, it hoped, make more profits)." *Winstar IV*, 518 U.S. at 851.

In the early 1980's, the Government required institutions to have five percent capital on hand to support outstanding loans. *See* Breeden, 59 *Fordham L.Rev.* at S75 (citing Net

Worth Amendment, 45 Fed.Reg. 76,111 (1980)). This was later reduced to four percent, and by January, 1982, the FHLBB reduced the capital requirements to three percent. *See id.* (citing Net Worth Amendment, 47 Fed.Reg. 3,543 (1982)). This had the effect of increasing a thrift's leveraging capacity to a ratio of over 33:1. *Id.* That is, for every one dollar of regulatory capital, a thrift could make thirty-three dollars worth of loans.

At three percent, the $217.5 million capital credit and the $79 million in supervisory goodwill together would have supported over nine billion dollars in additional loans. The supervisory goodwill that resulted from the merger would alone have supported over two and a half billion dollars in loans.

We believe it is clear that this leveraging opportunity was a crucial factor in the prospects of a successful rescue of the thrift. The Individual Plaintiffs' Bid Proposal specifically conditioned the offer to form SCH and SoCal and rescue the failing, insolvent thrift on the Government's approval of its goodwill proposal.

The Government's own internal documents, specifically a memorandum to the Bank Board urging the FHLBB to approve the SoCal transaction, dated two days before the Overall Contract documents were signed, indicate just as clearly that it was the Government's belief that the promises as to the capital credit and the treatment of the supervisory goodwill were necessary elements of the transaction.

> SoCal Holdings acquisition of Southern California is to be accounted as a purchase. Assets acquired and liabilities assumed will be adjusted and recorded at their fair values as of the acquisition date. Any excess of the fair value of the assets will be reflected as goodwill. The amortization of the resulting goodwill will be done over a 25 year period in accordance with the Applicant's re-

> quest for a Regulatory Accounting Principals ("RAP") exception. In addition, we recommend approval of the Applicant's request for RAP exception to allow the amount of the FSLIC assistance to count as a credit to SoCal Savings Bank's net worth. *These forbearances are critical to the transaction and business plan.*

Alvin W. Smuzynski Memo to the FHLBB, dated April 28, 1987, p. 3 (emphasis added).

This memorandum specifically notes that the FHLBB would be granting two regulatory exceptions to SoCal. Ignoring the relevance of this memorandum, the Government again attempts to raise the "missing promise" theory, arguing that the documents contain no specific promise allowing SoCal to count supervisory goodwill in meeting regulatory capital requirements.

The Smuzynski-FHLBB Memorandum, along with the Bid Proposal, serves as persuasive evidence of the parties' intent to contract for the treatment of SoCal's supervisory goodwill. As Judge Bruggink recently noted:

> If supervisory goodwill was not considered by the parties to be a capital asset for regulatory purposes, a contractual amortization schedule designed to eliminate it over time would have been completely unnecessary.

Home Sav., 50 Fed.Cl. at 437.

It is clear to this Court that, at the time the parties were negotiating and executing this transaction, they understood that supervisory goodwill would be included in regulatory capital. We see no basis for ascribing to words in the SoCal documents a meaning different from that given by a majority of the Supreme Court to identical words in the documents it interpreted. Accordingly, this final defense to the Defendant's breach is rejected as well.

V. CONCLUSION

This Court, like others before, has now addressed at length each of the Government's defenses, and has once again rejected them. Such an exercise was most certainly unnecessary, for as the seven Comparison Charts in the Appendix so vividly illustrate, the "facts and circumstances" in this case, a phrase oft-used by the Department of Justice in *Winstar*-related filings at the Court, are not at all different from those in the *Statesman* case. Accordingly, we are compelled to arrive at the same conclusions that other judges of this Court, the Federal Circuit, and the Supreme Court have all reached.

In his *Cal Fed* opinion addressing the issues common in these *Winstar* Short Form summary judgment motions, Senior Judge Smith wrote:

> In the instant cases the United States has not acted in a manner worthy of the great just Nation it is. Because the dollars at stake appear to be so large the government has raised legal and factual arguments that have little or no basis in law, fact or logic.
>
> While the court can appreciate the concerns of the government's attorneys to protect the public treasury, and they are honorable people, it must severely criticize the tactics and approach of the government in these motions for summary judgment.

Cal Fed. I, 39 Fed.Cl. at 754.

We have no reason to believe that then-Chief Judge Smith was unjustified in his harsh criticism of the Government's behavior as of 1997. Unfortunately, over four years later, the Government's tactics have not improved. Indeed, they have even less justification with the passage of time.

Fifteen years after the transactional documents were signed, the Court concludes that they established a valid, binding express contract between the Government, the Institutional

Plaintiffs, and the Individual Plaintiffs. The Government breached that contract when it enacted FIRREA, and with respect to two promises—the capital credit and supervisory goodwill. We do not, of course, mean to imply by these liability conclusions any particular quantum of recoverable damages. That we leave for the next phase.

We need not address Count 2 (breach of an implied-in-fact contract), Count 3 (breach of duty of good faith), or Count 4 (restitution for breach of contract). In 1999, then-Chief Judge Smith, in his capacity as *Winstar*-Managing Judge for the Court, stayed the Plaintiffs' constitutional claims. By an Order dated January 29, 2002, we denied the Defendant's motion to dissolve the stay on the Plaintiffs' constitutional claims, and thus we do not now reach Counts 5 (taking without just compensation) or 6 (due process violation).

Plaintiffs' Short Form Motion for Partial Summary Judgment is GRANTED as to Count 1, breach of an express contract, the Defendant's Cross Motion for Partial Summary Judgment is DENIED, and the case is continued for further proceedings to determine damages.

Pursuant to this Court's March 15, 2002, Order suspending the *Winstar* Amended Master Protective Order (AMPO) and lifting the seal off the files in this case, the Clerk of Court is directed to file this Opinion among the Court's public files. *See S. Cal. Fed. Sav. and Loan Assoc. v. United States*, 52 Fed.Cl. 20 (2002) *(AMPO Order)*.

IT IS SO ORDERED.

APPENDIX

Comparison Chart I

Statesman Documents	*Southern California* Documents
Statesman Assistance Agreement, "Accounting Principles" Clause—Section 17, March 11, 1988:	*SoCal* Assistance Agreement, "Accounting Principles" Clause—Section 13, April 30, 1987:
"Except as otherwise provided, any computations made for purposes of this Agreement shall be governed by GAAP, except that where such principles conflict with the terms of this Agreement, applicable regulations of the Bank Board or the [FSLIC], or any resolution or action of the Bank Board approving or relating to the Acquisition, the Mergers or to this Agreement, then this Agreement, such regulations, or such resolution or action shall govern.	"Except as otherwise provided herein, any computations made for the purposes of this Agreement shall be governed by GAAP as applied in the savings and loan industry, except that where such principles conflict with the terms of this Agreement, applicable regulations of the Bank Board or the [FSLIC], or any resolution or action of the Bank Board approving or relating to the Conversion, the Acquisition or this Agreement, then this Agreement, such regulations, or such resolution shall govern.
In the case of any ambiguity in the interpretation or construction of any provision of this Agreement, such ambiguity shall be resolved in a manner consistent with such regulations and the Bank Board's	In the case of any ambiguity in the interpretation or construction of any provision of this Agreement, such ambiguity shall be resolved in a manner consis-

resolution or action relating to the Acquisition. If there is a conflict between such regulations and the Bank Board's resolution or action relating to the Acquisition, the Mergers or to this Agreement, the Bank Board's resolution or action shall govern. For purposes of this section, the accounting principles and governing regulations shall be those in effect on the Effective Date, as subsequently changed, amended, clarified or interpreted by the Bank Board (as pro-posed, for example, at 52 *Fed. Reg.* 39112 *et seq.* (October 20, 1987)), its staff, or the Financial Accounting Standards Board ("FASB"), or any successor organization of the American Institute of Certified Public Accountants ("AICPA"). If there is a conflict between what is required by the FASB or the AICPA and what is required by the Bank Board, the interpretation of the Bank Board shall govern."	tent with such regulation and the Bank Board's resolution or action. If there is a conflict between such regulations and the Bank Board's resolutions or actions relating to the Conversion, the Acquisition or this Agreement, the Bank Board's resolutions or actions shall govern. For purposes of this Section, the accounting principles and governing regulations shall be those in effect on the Effective Date or as subsequently clarified or interpreted by the Bank Board or the Financial Accounting Standards Board ("FASB"), or any successor organization of the American Institute of Certified Public Accountants. Where there is a conflict between what is required by the FASB and the Bank Board, the interpretation of the Bank Board's accountants shall govern."

Comparison Chart II

Statesman Documents	*Southern California* Documents
Statesman Assistance Agreement, "Entire Agreement & Severability" Clauses-Section 23:	*SoCal* Assistance Agreement, "Entire Agreement & Severability" Clauses-Section 18:
"(a) This Agreement, together with any resolutions adopted by the Bank Board and documents delivered at closing which contain written interpretations or understandings of the parties, constitutes the entire agreement between the parties and supersedes all prior agreements and understandings of the parties in connection with it, excepting only the Acquisition Agreement, the Merger Agreements and any resolutions or letters concerning the Acquisition, the Mergers or this Agreement issued by the Bank Board or the [FSLIC] in connection with the approval of the Acquisition, the Mergers and this Agreement, *provided*, however, that in the event of any conflict, variance, or inconsistency between this Agreement	"(a) This Agreement, together with any interpretation or understanding agreed to in writing by the parties, constitutes the entire agreement between the parties and supersedes all prior agreements and understandings of the parties in connection with it, excepting only any resolutions or letters concerning the Conversion, the Acquisition or this Agreement issued by the Bank Board or the [FSLIC] in connection with the approval of the Conversion, the Acquisition, and this Agreement. [No Comparable Provision] (b) If any provision of this Agreement is invalid or unenforceable, all of the remaining provisions of this Agreement shall nevertheless remain in full

and the Acquisition Agreement or the Merger Agreements, the provisions of this Agreement shall govern and be binding on all parties insofar as the rights, privileges, duties, obligations, and liabilities of the parties are concerned. (b) If any provision of this Agreement is invalid or unenforceable, all of the remaining provisions of this Agreement shall nevertheless remain in full force and effect and shall be binding upon all the parties hereto."	force and effect and shall be binding upon the [FSLIC], the ACQUIRER and the NEW ASSOCIATION."

Comparison Chart III

Statesman Documents	*Southern California* Documents
Statesman Assistance Agreement, "Sole Benefit" Clause-Section 26: "It is the intention of the parties that this Agreement, the assumption of obligations and statements of responsibilities under it, and all of its conditions and provisions are for the sole benefit of the parties hereto and for the benefit of no other person.	*SoCal* Assistance Agreement, "Sole Benefit" Clause-Section 21: "It is the intention of the parties that this Agreement, the assumption of obligations and statements of responsibilities under it, and all of its conditions and provisions are for the sole benefit of the parties hereto and for the benefit of no other person.

Nothing expressed or referred to in this Agreement is intended or shall be construed to give any person other than the parties hereto any legal or equitable right, remedy, or claim under, or in respect to, this Agreement or any of its provisions."	Nothing expressed or referred to in this Agreement is intended or shall be construed to give any person other than the parties hereto any legal or equitable right, remedy, or claim under, or in respect to, this Agreement or any of its provisions."

Comparison Chart IV

<u>*Statesman* Documents</u>	<u>*Southern* California Documents</u>
Statesman Regulatory Capital Maintenance Agreement, March 11, 1998, Section 1:	*SoCal* Regulatory Capital Maintenance Agreement, April 30, 1987, Section 1:
"So long as the ACQUIRER directly or indirectly controls the ACQUIRING ASSOCIATION, as the term 'control' is defined in Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1987), or any successor regulation, as now or hereafter in effect, the ACQUIRER and the ACQUIRING ASSOCIATION shall cause the 'regulatory capital' as defined in § 561.13 of the Insurance Regulations, 12 C.F.R.	"So long as the ACQUIRER directly or indirectly controls the NEW ASSOCIATION, as the term "control" is defined in Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986), or any successor regulation, as now or hereafter in effect, the ACQUIRER and the NEW ASSOCIATION shall cause the 'regulatory capital' as defined in § 561.13 of the Insurance Regulations, 12 C.F.R. § 561.13 (1986), or any

§ 561.13 (1987), or any successor regulation, as now or hereafter in effect, of the ACQUIRING ASSOCIATION ("ACQUIRING ASSOCIATION's Regulatory Capital") to be maintained at the level ("Required Regulatory Capital") required by § 561.13(b) of the Insurance Regulations, 12 C.F.R. § 561.13(b) (1987), or any successor regulation, as now or hereafter in effect ("Regulatory Capital Regulation"), without regard to any net worth assistance for which the ACQUIRING ASSOCIATION may qualify pursuant to § 406 (f)(5) of the NHA, 12 U.S.C. § 1729(f)(5) (1982), as in effect now or as reenacted or amended in the future, and the regulations of the FSLIC issued pursuant to § 406(f)(5), or any successor regulation, as now or hereafter in effect.	successor regulation, as now or hereafter in effect,
[No Comparable Provision]	of the NEW ASSOCIATION to be maintained at the level required by § 561.13(b) of the Insurance Regulations, 51 Fed.Reg. 33,565 (1986) (to be codified at 12 C.F.R. § 561.13(b) (1987), or any successor regulation, as now or hereafter in effect ("Regulatory Capital Regulation") ("Required Regulatory Capital"), without regard to any net worth assistance for which the NEW ASSOCIATION may qualify pursuant to § 406(f)(5) of the NHA, 12 U.S.C. § 1729(f)(5) (1982), and the regulations of the [FSLIC] issued pursuant to § 406(f)(5), or any successor statute or regulations, as now or hereafter in effect, *provided* that for the purposes of § 561.13(b) of the Regulatory Capital Regulations, (i) the [FSLIC], pursuant to its authority under § 563.13(b)(7)(iii) of the Regulatory Capital Regulation, shall consider the NEW ASSOCIATION's
[No Comparable Provision]	
The form of any capital infusion required by this § 1	

must be acceptable to the Principal Supervisory Agent of the Bank Board, Des Moines, Iowa, or his designee ("P.S.A.")."	'base liabilities,' as defined in § 563.13(b)(1)(ii) of the Regulatory Capital Regulation, to be the lower of the NEW ASSOCIATION's level ". . . of 'total liabilities,' as defined in § 563.13(b)(1)(i) of the Regulatory Capital Regulation ("Total Liabilities"), as of (A) the effective date of the acquisition (end of the day) and (B) the end of the period for which regulatory capital is being computed, and (ii) the [FSLIC], pursuant to its authority under § 563.13(b)(7)(iii) of the Regulatory Capital Regulation, shall consider the NEW ASSOCIATION's 'base ratio,' as defined in § 563.13(b)(2)(iii) of the Regulatory Capital Regulation, to be 3 percent, and *provided further*, that regardless of any changes in the method of calculating regulatory capital or the items includable in such calculation, the $217.5 million of assistance from the [FSLIC] shall be includable in capital for purposes of determining whether the

	NEW ASSOCIATION has maintained its regulatory capital at the Required Regulatory Capital level. The form of any capital infusion required by this § 1 must be acceptable to the Principal Supervisory Agent of the Bank Board, San Francisco, California, or his designee ("P.S.A.").

Comparison Chart V

Statesman Documents	*Southern California* Documents
Statesman RCMA, Section 2: "For purposes of this Agreement, any determination of the ACQUIRING ASSOCIATION's Required Regulatory Capital shall be calculated by the FSLIC or the P.S.A., and shall include in the ACQUIRING ASSOCIATION's Required Regulatory Capital amounts permitted by the FSLIC in the Assistance Agreement and in the forbearances issued in connection with the transactions discussed therein."	*SoCal* RCMA, Section 2: "For purposes of this Agreement, any computation of the NEW ASSOCIATION's Required Regulatory Capital shall be determined by the P.S.A., in accordance with applicable regulations, standards and procedures generally applicable to institutions under the P.S.A.'s jurisdiction and the second proviso of § 1, and shall reflect any directives issued by the P.S.A., in accordance with such regulations, standards and procedures and the second proviso of § 1, regarding

	the NEW ASSOCIATION's calculation of Required Regulatory Capital."

Comparison Chart VI

Statesman Documents	*Southern California* Documents
Statesman FHLBB Resolution No. 88-169, March 11, 1998:	*SoCal* FHLBB Resolution No. 87-511, April 30, 1987:
"RESOLVED FURTHER, That the Acquisition and the Mergers shall be accounted for, and [Statesman] shall report to the Bank Board and the FSLIC, in accordance with generally accepted accounting principles prevailing in the savings and loan industry, as accepted, modified, clarified, or interpreted by applicable regulations of the Bank Board and the FSLIC, except to the extent of the following departures from generally accepted accounting principles:	"RESOLVED FURTHER, That SoCal Holdings and the New Association shall submit to the Principal Supervisory Agent an independent certified public accountant's opinion that each has accounted for the Acquisition in accordance with generally accepted accounting principles ("GAAP") or in accordance with GAAP as it may be modified by the following procedures, which shall be employed:
[No Comparable Provision]	(a) Push-down accounting shall be used to reflect the Acquisition on the books of the New Association;
(a) Twenty-one million dollars of the initial contribution by the [FSLIC]	(b) The cash contribution by the FSLIC to the New Association, pursuant to

to [Statesman], and five million dollars of the principal amount of the Subordinate Debenture issued to the FSLIC, pursuant to § 6 of the Assistance Agreement, shall be credited to the regulatory capital account of [Statesman]; and (b) The value of any unidentifiable intangible assets resulting from accounting for the Acquisition in accordance with the purchase method of accounting may be amortized by [Statesman] over a period not in excess of twenty-five (25) years by the straight line method."	the Assistance Agreement, may be deemed a contribution to regulatory capital and may be booked as a direct credit to the New Association's regulatory capital; and (c) The value of any intangible assets resulting from the Acquisition shall be amortized by the New Association over a period not to exceed 25 years by the straight line method."

Comparison Chart VII

Statesman Documents	*Southern California* Documents
Statesman Forbearance Letter, March 14, 1988: "In connection with approval by the [FHLBB] of the assisted transaction of [thrifts to be acquired] by [Statesman] . . . the following forbearances are hereby granted:	*SoCal* Forbearance Letter, May 27, 1987: "Concurrent with the approval of the [SoCal] transaction, the following forbearances are granted: 1. The assets acquired by [SoCal] . . . will be deemed to have been acquired in an acquisition instituted for

1. The acquisition of control of the associations by [Statesman] has been deemed to be an acquisition instituted for supervisory reasons. Therefore, the [FSLIC] will forbear, for a period not to exceed five years following consummation of the acquisition, from exercising its authority under Section 563.13 of the Insurance Regulations, for any failure of [Statesman] to meet the regulatory capital requirements. . . . 3. It is the FSLIC's intention [sic] $21 million of the case contribution to be made to [Statesman] pursuant to an assistance agreement to be entered intro between the FSLIC and [Statesman] and the $5 million subordinated debenture are to be a credit to [Statesman's] regulatory capital; therefore, for regulatory accounting purposes, [Statesman] may book such contribution as a direct addition to its regulatory capital.	supervisory reasons. Therefore, pursuant to any section of the regulations administered by the [FHLBB] . . . scheduled items attributable to [SoCal] shall be excluded from the computation of scheduled items in determining whether [SoCal] meets the requirements of such sections following the effective acquisition date. 2. Not later than 60 days following the effective date of the acquisition, [SoCal] shall submit to the Supervisory Agent an independent certified public accountant's opinion that [SoCal] has accounted for the acquisition in accordance with generally accepted accounting principles ("GAAP"), or in accordance with GAAP except to the extent that the following may depart from GAAP and which is hereby approved by the Board for purposes of regulatory reporting by [SoCal] to the Board: (a) the cash contribution by the FSLIC to [SoCal] with

4. Not later than 90 days following the effective date of the merger, [Statesman] shall submit to the Supervisory Agent an independent certified public accountant's opinion that [Statesman] has accounted for the merger in accordance with generally accepted accounting principles except that as herein provided by the Board, for purposes of reporting to the Board the cash contribution by the FSLIC to [Statesman] with respect to the associations, pursuant to the assistance agreement, and the $5 million subordinated debenture shall be booked as a direct credit to [Statesman]."	respect to [SoCal] pursuant to the Assistance agreement shall be deemed a contribution to regulatory net worth, and may be booked as a direct credit to [SoCal], (b) the value of any unidentifiable intangible assets resulting from accounting for the acquisition in accordance with the purchase method may be amortized by SoCal Federal over a period not exceed 25 years by the straight line method."

APPENDIX D

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

04-5036, -5038

SOUTHERN CALIFORNIA FEDERAL SAVINGS & LOAN ASSOCIATION and SOCAL HOLDINGS, INC.,
Plaintiffs-Appellees,

ARBUR, INC., WILLIAM E. SIMON, JR., J. PETER SIMON, and GEORGE J. GILLESPIE, III (Executors of the Estate of William E. Simon, Sr.) and ROY DOUMANI, PRESTON MARTIN, and BEVERLY W. THRALL (Successor to the Claims of Larry B. Thrall),
Plaintiffs-Cross Appellants,

v.

UNITED STATES,
Defendant-Appellant.

ORDER

The petitions for panel rehearing and for rehearing en banc having been filed by the APPELLEES (Arbur, Inc., *et al.*), and by the CROSS-APPELLANTS, and responses thereto having been invited by the court and filed by the APPELLANT, and the petitions for rehearing having been referred to the panel that heard the appeals, and thereafter the petitions for rehearing en banc and responses having been referred to the circuit judges who are in regular active service,

UPON CONSIDERATION THEREOF, it is

ORDERED that the petitions for panel rehearing be, and the same hereby are, DENIED and it is further

ORDERED that the petitions for rehearing en banc be, and the same hereby are, DENIED.

The mandate of the court will issue on January 3, 2006.

FOR THE COURT,
Jan Horbaly, Clerk

Dated: December 27, 2005

APPENDIX E

[JX 1428]

REGULATORY CAPITAL MAINTENANCE AGREEMENT AMONG SOCAL HOLDINGS, INC., WILLIAM E. SIMON, ARBUR, INC., GERALD L. PARSKY, LARRY B. THRALL, ROY DOUMANI, PRESTON MARTIN, AND CRAIG GOSDEN, SOUTHERN CALIFORNIA FEDERAL SAVINGS AND LOAN ASSOCIATION,

AND

THE FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

DATED April 30, 1987

TABLE OF CONTENTS

		Page
Recitals		1
§ 1.	Regulatory Capital Maintenance by the ACQUIRER and the NEW ASSOCIATION	3
§ 2.	Computation of Required Regulatory Capital and Amendment of Regulatory Capital Regulation	4
§ 3.	Waiver of Net Worth Assistance	5
§ 4.	Guarantees by the ACQUIRING GROUP	5
§ 5.	Covenants of the ACQUIRER, ACQUIRING GROUP and NEW ASSOCIATION	6
§ 6.	Irrevocable Proxy	10
§ 7.	CORPORATION's Voting and Disposition Rights	10
§ 8.	Termination of Certain Provisions	13
§ 9.	Specific Performance	14
§ 10.	Notices	15
§ 11.	Rights and Forbearances	16
§ 12.	Governing Law	16
§ 13.	Entire Agreement, Severability	17
§ 14.	Counterparts, Modifications, Headings	17
§ 15.	Successors and Assigns	18
Signature Page		18

REGULATORY CAPITAL MAINTENANCE AGREEMENT

THIS AGREEMENT, dated April 30, 1987, is entered into by and among SoCAL Holdings, Inc., a savings and loan holding company incorporated under the laws of the State of Delaware ("ACQUIRER"); William E. Simon, Arbur, Inc., a Delaware corporation owned by Mr. Simona and his children, Gerald L. Parsky, Larry B. Thrall, Roy Doumani, Preston Martin and Craig Gosden (collectively, "ACQUIRING GROUP"); Southern California Federal Savings and Loan Association, a federally-chartered stock savings and loan association, Beverly Hills, California ("NEW ASSOCIATION"); and the Federal Savings and Loan Insurance Corporation, a corporate instrumentality of the United States ("CORPORATION").

RECITALS

A. The members of the ACQUIRING GROUP collectively own 97.5 percent of the outstanding voting securities of the ACQUIRER and "control" the ACQUIRER, as that term is used in Part 574 of the Regulations for the Federal Savings and Loan Insurance Corporation ("Insurance Regulations"), 12 C.F.R. Part 574 (1986).

B. The Federal Home Loan Bank Board ("Bank Board"), by Resolution No. 87-511, dated April 30, 1987, authorized the supervisory conversion of Southern California Federal Savings and Loan Association, Beverly Hills, California, a federally-chartered mutual savings and loan association, into the NEW ASSOCIATION, and authorized the purchase by the ACQUIRER of all of the NEW ASSOCIATION's common stock.

C. THE ACQUIRER, pursuant to a Stock Purchase Agreement of even date herewith, has agreed to purchase all of the shares of common stock to be initially issued by the NEW ASSOCIATION ("Acquisition").

D. The CORPORATION has decided, pursuant to § 406(f)(1)-(4) of the National Housing Act, as amended ("NHA"), 12 U.S.C. § 1729(f)(1)-(4) (1982), to provide financial assistance and indemnification in connection with the ACQUIRER's purchase of the NEW ASSOCIATION's common stock as set forth in an Assistance Agreement of even date herewith among the ACQUIRER, the NEW ASSOCIATION and the CORPORATION.

E. A condition of the obligation of the CORPORATION to provide financial assistance and indemnification as set forth in the Assistance Agreement is that the ACQUIRER, the ACQUIRING GROUP and the NEW ASSOCIATION enter into an agreement in the form of this Agreement, pursuant to which the CORPORATION will receive certain assurances and rights with respect to maintenance of the regulatory capital of the NEW ASSOCIATION.

F. In consideration of the mutual promises contained herein, the parties enter into the following agreement.

G. The CORPORATION in the Assistance Agreement has agreed that the $217.5 million of assistance provided by the CORPORATION in connection with the Acquisition would be includable in capital for regulatory accounting purposes regardless of any changes made in the calculation of or items includable in regulatory capital, including any requirement that regulatory capital be calculated in accordance with generally accepted accounting principles.

AGREEMENT

§ 1. *Regulatory Capital Maintenance by the ACQUIRER and the NEW ASSOCIATION.* So long as the ACQUIRER directly or indirectly controls the NEW ASSOCIATION, as the term "control" is defined in Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986), or any successor regulation, as now or hereafter in effect, the ACQUIRER and the NEW ASSOCIATION shall cause the "regulatory capi-

tal," as defined in § 561.13 of the Insurance Regulations, 12 C.F.R. § 561.13 (1986), or any successor regulation, as now or hereafter in effect, of the NEW ASSOCIATION to be maintained at the level required by § 563.13(b) of the Insurance Regulations, 51 Fed. Reg. 33,565 (1986) to be codified at 12 C.F.R. § 563.13(b) (1987)), or any successor regulation, as now or hereafter in effect ("Regulatory Capital Regulation") ("Required Regulatory Capital"), without regard to any net worth assistance for which the NEW ASSOCIATION may qualify pursuant to § 406(f)(5) of the NHA, 12 U.S.C. § 1729(f)(5) (1982), and the regulations of the CORPORATION issued pursuant to § 406(f)(5), or any successor statute or regulations, as now or hereafter in effect, *provided* that for purposes of § 563.13(b) of the Regulatory Capital Regulation, (i) the CORPORATION, pursuant to its authority under § 563.13(b)(7)(iii) of the Regulatory Capital Regulation, shall consider the NEW ASSOCIATION's "base liabilities," as defined in § 563.13(b)(1)(iii) of the Regulatory Capital Regulation, to be the lower of the NEW ASSOCIATION's level of "total liabilities," as defined in § 563.13(b)(1)(i) of the Regulatory Capital Regulation ("Total Liabilities"), as of (A) the effective date of the Acquisition (end of the day) and (B) the end of the period for which regulatory capital is being computed, and (ii) the CORPORATION, pursuant to its authority under § 563.13(b)(7)(iii) of the Regulatory Capital Regulation, shall consider the NEW ASSOCIATION's "base ratio," as defined in § 563.13(b)(2)(iii) of the Regulatory Capital Regulation, to be 3 percent, and *provided further*, that regardless of any changes in the method of calculating regulatory capital or the items includable in such calculation, the $217.5 million of assistance from the CORPORATION shall be includable in capital for purposes of determining whether the NEW ASSOCIATION has maintained its regulatory capital at the Required Regulatory Capital level. The form of any capital infusion required by this § 1 must be acceptable to the

Principal Supervisory Agent of the Bank Board, San Francisco, California, or his designee ("P.S.A.").

§ 2. *Computation of Required Regulatory Capital and Amendment of Regulatory Capital Regulation.* For purposes of this Agreement, any computation of the NEW ASSOCIATION'S Required Regulatory Capital shall be as determined by the P.S.A., in accordance with applicable regulations, standards and procedures generally applicable to institutions under the P.S.A.'s jurisdiction and the second proviso of § 1, and shall reflect anydirectives issued by the P.S.A., in accordance with such regulations, standards and procedures and the second proviso of § 1, regarding the NEW ASSOCIATION's calculation of Required Regulatory Capital.

§ 3. *Waiver of Net Worth Assistance.* The ACQUIRER and the NEW ASSOCIATION hereby waive any right to any net worth assistance for which the NEW ASSOCIATION may qualify pursuant to § 406(f)(5) of the NHA, 12 U.S.C. § 1729(f)(5) (1982), and the regulations of the CORPORATION issued thereunder, or any successor statute or regulations, as now or hereafter in effect.

§ 4. *Guarantees by the ACQUIRING GROUP.* Unless earlier terminated in accordance with § 8, so long as the ACQUIRER shall be obligated pursuant to § 1, the members of the ACQUIRING GROUP, severally in proportion to their initial ownership of the common stock of the ACQUIRER as reflected in the percentages set forth opposite their signatures below, hereby guarantee the performance of the ACQUIRER and the NEW ASSOCIATION under § 1, *provided* that the guarantees of Messrs. Simon and Parsky shall be joint and several to the extent of their combined initial ownership of the common stock, and *provided further*, that the personal obligations of the members of the ACQUIRING GROUP under said guarantees shall not exceed $5,000,000 in the aggregate. For these purposes, Mr. Simon shall be deemed to own the shares of common stock of the ACQUIRER actually

owned by Arbur, Inc. In addition, the guarantee of any member of the ACQUIRING GROUP shall be reduced proportionately or terminate to the extent he transfers any of his shares of common stock of the ACQUIRER to: (a) another member of the ACQUIRING GROUP, in which case such other member's guarantee shall be deemed to have been increased proportionately or (b) to any other person to the extent such person assumes the proportionate share of the guarantee and the CORPORATION shall not have reasonably objected to such person's ability to perform such guarantee within 30 days of notice of the transfer (whether such notice is given prior to or after such transfer), which notice shall include sufficient financial information with respect to the transferee in order to enable the CORPORATION to make an informed judgment with respect to such transferee's ability to perform the guarantee.

§ 5. Covenants of the ACQUIRER, ACQUIRING GROUP and NEW ASSOCIATION. Unless the CORPORATION consents or otherwise agrees, in either case in writing:

(a) The ACQUIRER will not, directly or indirectly, through one or more transactions, issue any voting securities, stock options, warrants, or other instruments or obligations convertible into voting securities of the ACQUIRER or which, upon the occurrence of one or more events, may acquire any voting rights with respect to the ACQUIRER, to any person or entity other than members of the ACQUIRING GROUP unless the ACQUIRER discloses the provisions of this Agreement to such person or entity prior to such transaction and (i) the exercisability or convertibility of such securities, options, warrants, instruments or obligations is conditioned upon obtaining approval from the CORPORATION or (ii) if after giving effect to such transaction and the issuance of voting securities issuable upon conversion or exercise of any securities, options, warrants, other instruments or obligations of the ACQUIRER, the ACQUIRING GROUP would own at

least a majority of the outstanding voting power of the ACQUIRER, *provided, however*, that voting securities issuable upon conversion or exercise of securities, the conversion or exercisability of which is conditioned upon some event or action within the control of the ACQUIRING GROUP, the ACQUIRER or the NEW ASSOCIATION, shall not be deemed outstanding for these purposes. It is understood that nothing contained herein shall inhibit the Acquirer's ability to issue securities which have no voting rights or which are not convertible into or exercisable for the acquisition of securities with voting rights;

(b) No member of the ACQUIRING GROUP shall sell, assign, give, transfer, exchange, pledge or otherwise dispose of or encumber any or all of his or its shares of voting stock of the ACQUIRER, nor any interest therein, unless the proposed transferee of such shares agrees to be bound by the provisions of this Agreement, other than § 4 (unless such transferee assumes, without objection by the CORPORATION, some or all of the transferor's guarantee under § 4), as if such transferee were a member of the ACQUIRING GROUP;

(c) The members of the ACQUIRING GROUP shall collectively own not less than a majority of the outstanding voting power of the ACQUIRER;

(d) The ACQUIRER's charter and bylaws shall provide for the removal of directors at any time, with or without cause;

(e) The ACQUIRER's charter and bylaws shall not require, nor shall the ACQUIRER be organized in any jurisdiction the law of which requires, the affirmative vote of more than a majority of the voting power of the ACQUIRER to approve any merger, consolidation, disposition of all or substantially all of the assets of the ACQUIRER or any similar extraordinary transaction involving the ACQUIRER ("Ex-

traordinary Acquirer Transaction") or to amend its charter or bylaws;

(f) The ACQUIRER shall retain ownership of 100 percent of the voting securities of the NEW ASSOCIATION and shall not cause or permit any merger, consolidation, disposition of all or substantially all of the assets of the NEW ASSOCIATION or any similar extraordinary transaction involving the NEW ASSOCIATION ("Extraordinary New Association Transaction");

(g) The NEW ASSOCIATION will not, directly or indirectly, through one or more transactions, issue any voting securities, stock options, warrants or other instruments or obligations convertible into voting securities of the NEW ASSOCIATION or which, upon the occurrence of one or more events, may acquire any voting rights with respect to the NEW ASSOCIATION, to any person or entity other than the ACQUIRER or members of the ACQUIRING GROUP;

(h) The NEW ASSOCIATION's charter and bylaws shall provide the right to remove any or all of the directors of the NEW ASSOCIATION, with or without cause; and

(i) Each instrument or certificate evidencing shares of voting securities of the ACQUIRER owned by any member of the ACQUIRING GROUP, and such securities transferred by any member of the ACQUIRING GROUP or any donee, transferee, or assignee thereof, shall be stamped or imprinted with a legend in the following form:

> "The securities represented by this certificate (a) may not be sold, transferred or otherwise disposed of except in compliance with the restrictions contained in a Regulatory Capital Maintenance Agreement dated as of April 30, 1987 among the Company and the parties named therein (a copy of which Agreement is available for inspection at the principal offices of the Company), (b) are subject to an irrevocable proxy as set forth in such

Agreement, and (c) are subject to certain other terms, provisions, options and rights, including a prohibition on pledges and other restrictions on transfer included in such Agreement and the possibility of forfeiture."

In the event of a violation of any of the covenants set forth in this § 5, the CORPORATION shall have the right to proceed as set forth in § 7 as if the NEW ASSOCIATION's regulatory capital had fallen below 3 percent of Total Liabilities as of the date of such violation.

§ 6. *Irrevocable Proxy.* Concurrently with the execution of this Agreement, each member of the ACQUIRING GROUP shall execute and deliver to the CORPORATION an irrevocable proxy in the form attached hereto as Exhibit A ("Irrevocable Proxy"). The Irrevocable Proxies shall be held by the Sectary to the Bank Board ("Secretary") on behalf of the CORPORATION. Until such time as the CORPORATION invokes its rights under § 7, subject to the other provisions of this Agreement, all rights related to the voting securities of the ACQUIRER initially owned by members of the ACQUIRING GROUP shall be retained by members of the ACQUIRING GROUP or their transferees.

§ 7. *CORPORATION'S Voting and Disposition Rights.* If the regulatory capital of the NEW ASSOCIATION shall, at the end of any month, fall below 3 percent of Total Liabilities and such deficiency shall not have been eliminated by the date of the filing of the NEW ASSOCIATION's Monthly Report for such month with the Bank Board, the CORPORATION, acting through the P.S.A., the Director of the Office of the Federal Savings and Loan Insurance Corporation ("OFSLIC") or the Director of the Office of Regulatory Policy, Oversight and Supervision ("ORPOS"), shall have the right to send a notice ("Notice") to the ACQUIRER and members of the ACQUIRING GROUP that the CORPORATION is invoking the provisions of this § 7. In the event that the NEW ASSOCIATION's Monthly Report for such

month does not reflect such deficiency, the Notice shall include a statement and accounting support for the determination that the regulatory capital level has fallen below the 3 percent requirement. The ACQUIRER shall have 15 days from the date of receipt of the Notice in which to file a rebuttal to the position taken in the Notice and the matter shall be resolved by the Bank Board, in its sole discretion, in a written finding. Alternatively, if the ACQUIRER does not dispute the Notice or the NEW ASSOCIATION's Monthly Report for such month reflects the inadequacy in regulatory capital, the ACQUIRER shall have 15 days from the date of receipt of the Notice in which to cure such deficiency. If the ACQUIRER has disputed the Notice, but the Bank Board has agreed with the determination set forth in the Notice, then the ACQUIRER shall have 7 days from the receipt of such written determination by the Bank Board in which to cure the deficiency. In such event, immediately upon receipt of such written determination by the Bank Board, or, in the event the ACQUIRER does not dispute the Notice or the NEW ASSOCIATION's Monthly Report reflects the inadequacy in regulatory capital, immediately upon receipt of the Notice, each member of the ACQUIRING GROUP shall forward to the Secretary, by overnight delivery or comparable means, the certificates representing all of the voting securities of the ACQUIRER then owned by that member of the ACQUIRING GROUP, properly endorsed for transfer or accompanied by fully endorsed stock powers. Unless the deficiency referred to in the first sentence of this § 8 is eliminated within the appropriate time period provided in this § 8, the CORPORATION, acting through the P.S.A., the Director of OFSLIC, or the Director of ORPOS, in any case with the concurrence of the Office of the General Counsel ("OGC"), shall have the absolute right, acting pursuant to a Bank Board

resolution specifically authorizing such action and otherwise in its sole discretion, to:

(a) vote pursuant to the Irrevocable Proxy all voting securities of the ACQUIRER subject to the terms of this Agreement, including, without limitation, the exercise of such voting power:

(1) in favor of, and causing the taking of such steps as may be necessary to consummate, an Extraordinary Acquirer Transaction, an Extraordinary New Association Transaction or the sale of any or all of the NEW ASSOCIATION's voting securities, even if no value is received in respect of the voting securities of the ACQUIRER subject to this Agreement or the net assets of the ACQUIRER or the securities or net assets of the NEW ASSOCIATION; and/or

(2) the removal of the board of directors of the ACQUIRER and/or the NEW ASSOCIATION; and/or

(3) causing the ACQUIRER or the NEW ASSOCIATION to issue to the CORPORATION or another party or parties designated by the CORPORATION, in its sole discretion, for nominal or no consideration, voting securities representing a majority of the voting power of the ACQUIRER or the NEW ASSOCIATION after such issuance; and/or

(b) dispose of any or all of the voting securities of the ACQUIRER subject to this Agreement, even if no value is received in respect of such securities.

In the event of any such transaction or disposition, the owners of voting securities of the ACQUIRER or the NEW ASSOCIATION, as the case may be, shall be entitled to the consideration, if any, paid in respect of such securities less each such person's proportionate share of the costs associated

with the transaction or disposition including, without limitation, any financial assistance provided by the CORPORATION in connection with such transaction or disposition.

§ 8. *Termination of Certain Provisions.* The guarantees provided for in § 4, the covenants set forth in § 5, the Irrevocable Proxy, and the provisions of § 7 shall terminate on the earliest of the following:

(a) The expiration of 12 years from the date of this Agreement;

(b) The delivery to the CORPORATION of a perpetual guarantee of the NEW ASSOCIATION's regulatory capital, in form and substance satisfactory to the CORPORATION and signed by or on behalf of one or more guarantors acceptable to the CORPORATION; or

(c) If, at the request of the NEW ASSOCIATION, the P.S.A. determines that the NEW ASSOCIATION maintains for a period of 12 consecutive quarters after the expiration of 5 years from the date of this Agreement a ratio of "tangible net worth", as defined below, to Total Liabilities of at least 6-1/2%. For purposes of this § 8(c), "tangible net worth" means net worth as determined in accordance with generally accepted accounting principles minus goodwill and other intangible assets and does not include either (i) any form of subordinated debt or (ii) any preferred stock that (A) is not included in regulatory capital pursuant to the Regulatory Capital Regulation, (B) has a stated maturity, (C) includes mandatory redemption provisions, (D) must be redeemed by the NEW ASSOCIATION at the option of the holder, or (E) has a dividend rate that increases or can increase in such a manner as to effectively require the NEW ASSOCIATION to redeem the preferred stock.

All determinations of the CORPORATION required by this § 8 shall be made by the P.S.A., the Director of OFSLIC, or

the Director of ORPOS, in each case with the concurrence of OGC.

§ 9. *Specific Performance.* The ACQUIRER, the NEW ASSOCIATION and members of the ACQUIRING GROUP acknowledge and agree that the rights reserved to the CORPORATION hereunder are of a special, unique, unusual and extraordinary character, which gives them a peculiar value, the loss of which cannot be adequately or reasonably compensated for in damages in an action at law, and the breach by any of the ACQUIRER, the NEW ASSOCIATION and members of the ACQUIRING GROUP of any of the provisions hereof will cause the CORPORATION irreparable injury and damage. In such event, the CORPORATION shall be immediately entitled, as a matter of right, to require of the defaulting party specific performance of all of the acts and undertakings required hereunder, including the obtaining of all requisite authorizations to execute or perform this Agreement and to obtain injunctive and other equitable relief in any court of competent jurisdiction (including, without limitation, the United States District Court for the District of Columbia) to prevent the violation or threatened violation of any of the provisions hereof. Neither this provision nor any exercise by the CORPORATION of rights to equitable relief or specific performance herein granted shall constitute a waiver of any other rights which it may have to damages or otherwise.

§ 10. *Notices.*

(a) Any notices or other communication required or permitted under this Agreement, unless otherwise specifically provided for, shall be deemed given when delivered if delivered personally or by U.S. Express Mail or commercial overnight courier service or three business days after posting if sent by first class mail, postage prepaid, to a party at its

address set forth below or at such other address as the party shall furnish in writing:

If to the ACQUIRER:
SoCAL Holdings, Inc.
c/o Preston Martin
One Montgomery Street, West Tower
San Francisco, California 94104

If to the New ASSOCIATION:
Southern California Federal Savings
and Loan Association
Attn: President
9100 Wilshire Boulevard
Beverly Hills, California 90212

If to the ACQUIRING GROUP:
c/o Gerald L. Parsky
333 South Grand Avenue
Los Angeles, California 90071

If to the CORPORATION:
FEDERAL SAVINGS AND LOAN INSURANCE
CORPORATION
Attn: Director, Financial Assistance Division
1700 G Street, N.W.
Washington, D.C. 20552

(b) Unless otherwise specifically provided for, if this Agreement requires that notice be given within a certain period of time, notice shall be deemed given as of the date of posting.

§ 11. *Rights and Forbearances.* The rights, powers, and remedies given to the parties by this Agreement shall be in addition to all rights, powers, and remedies given by any applicable statute or rule of law. Any forbearance, failure, or delay by any party in exercising or partially exercising any

such right, power, or remedy shall not preclude its further exercise.

§ 12. *Governing Law.* To the extent that Federal law does not control, this Agreement and the parties' rights and obligations under it shall be governed by the law of the State of Delaware. Nothing in this Agreement shall require any unlawful action or inaction by either party.

§ 13. *Entire Agreement; Severability.*

(a) This Agreement, together with any interpretation or understanding agreed to in writing by the parties, constitutes the entire agreement among the parties and supersedes all prior agreements and understandings of the parties in connection with the subject matter hereof.

(b) If any provision of this Agreement is invalid or unenforceable, all of the remaining provisions of this Agreement shall nevertheless remain in full force and effect and shall be binding upon the CORPORATION, the ACQUIRER, the NEW ASSOCIATION and the ACQUIRING GROUP.

§ 14. *Counterparts, Modifications, Headings.*

(a) This Agreement and the Irrevocable Proxy may be executed in any number of counterparts, each of which shall be an original, but all of which shall constitute one and the same instrument, and any party may execute this Agreement or the Irrevocable Proxy by signing any such counterpart.

(b) No amendment or modification of this Agreement shall be binding unless executed in writing by all the parties or their successors.

(c) Section headings are not to be considered part of this Agreement, are solely for convenience of reference, and shall not affect the meaning or interpretation of this Agreement or any of its provisions.

§ 15. *Successors and Assigns.* All the terms and provisions of this Agreement shall be binding upon and inure to the benefit of the parties and their respective transferees, successors and assigns.

IN WITNESS WHEREOF, the parties have executed this Agreement or caused it to be executed on their behalf by their duly authorized officers or agents.

ATTEST: SOCAL HOLDINGS, INC.
By: By:
Its: Its:

ATTEST: SOUTHERN CALIFORNIA FEDERAL SAVINGS AND LOAN ASSOCIATION
By: By:
Its: Its:

ATTEST: William E. Simon (19.4%)

ATTEST: ARBUR, INC. (9.6%)
By: By:
Its: Its:

ATTEST: Gerald L. Parsky (29%)

ATTEST: Larry B. Thrall (14%)

ATTEST: Roy Doumani (14%)

ATTEST: Preston Martin (7.5%)

ATTEST: Craig Gosden (4%)

ATTEST: FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION
By: By:
Its: Its:

EXHIBIT A

IRREVOCABLE PROXY

The undersigned agree to and do hereby grant to the Federal Savings and Loan Insurance Corporation, a corporate instrumentality of the United States ("FSLIC"), an irrevocable proxy pursuant to the provisions of Section 212 of the Delaware General Corporation Law to vote, or to execute and deliver written consents or otherwise act with respect to, all voting securities (the "Stock") of SoCal Holdings, Inc. (the "Company") now owned or hereafter acquired by the undersigned as fully, and to the same extent and with the same effect, as the undersigned might or could do under any applicable laws or regulations governing the rights and powers of stockholders of a Delaware corporation, in accordance with, and as provided in, a certain Regulatory Capital Maintenance Agreement, dated April 30, 1987, among the undersigned, the Company, Southern California Federal Savings and Loan Association, and the FSLIC. The undersigned hereby affirm that this proxy is given as a condition of said Regulatory Capital Maintenance Agreement and in connection with the acquisition of Southern California Federal Savings and Loan Association by the Company and as such is coupled with an interest and is, therefore, irrevocable. This proxy may be exercised by the Principal Supervisory Agent of the Federal Home Loan Bank Board ("Bank Board"), San Francisco, California, the Director of the Office of the FSLIC, or the Director of the Office of Regulatory Policy, Oversight and Supervision of the Bank Board, with the concurrence of the Office of the General Counsel of the Bank Board upon authorization by a resolution of the Bank Board as provided in said Regulatory Capital Maintenance Agreement at any meeting of the stockholders of the Company or in any action of such stockholders without a meeting

until April 29, 1999, unless sooner terminated in accordance with the provisions of said Regulatory Capital Maintenance Agreement.

THIS PROXY SHALL REMAIN IN FULL FORCE AND EFFECT UNTIL APRIL 29, 1999 UNLESS SOONER TERMINATED IN ACCORDANCE WITH THE PROVISIONS OF THE REGULATORY CAPITAL MAINTENANCE AGREEMENT DATED APRIL 30, 1987 AMONG THE FSLIC, THE COMPANY AND CERTAIN STOCKHOLDERS OF THE COMPANY AND SHALL BE ENFORCEABLE AGAINST ANY DONEE, TRANSFEREE OR ASSIGNEE OF THE STOCK.

Dated this 30th day of April, 1987

William E. Simon
ARBUR, INC.
By:
Its:
Gerald L. Parsky
Larry B. Thrall
Roy Doumani
Preston Martin
Craig Gosden

APPENDIX F

[JX 1425]

FEDERAL HOME LOAN BANK BOARD

Supervisory Conversion of
Southern California Federal
Savings and Loan Association,
Beverly Hills, California, and Acquisition by
SoCal Holdings, Inc., San Francisco, California

No. 87-511
Date: April 30, 1987

Recitals

WHEREAS, Southern California Federal Savings and Loan Association, Beverly Hills, California ("SoCal"), is a federally-chartered mutual savings and loan association, the accounts of which are insured by the Federal Savings and Loan Insurance Corporation ("FSLIC"); and

WHEREAS, SoCal Holdings, Inc., San Francisco, California ("SoCal Holdings"), is a savings and loan holding company organized under the laws of the State of Delaware for the purpose of acquiring SoCal upon its conversion to the federal stock savings and loan association form; and

WHEREAS, SoCal, upon its conversion to the federal stock savings and loan association form, will continue to be known as Southern California Savings and Loan Association") ("New Association"); and

WHEREAS, William E. Simon, Arbur, Inc., a Delaware corporation owned by Mr. Simon and his children, Gerald L. Parsky, Larry B. Thrall, Roy Doumani, Preston Martin and Craig Gosden are the common stockholders of SoCal Holdings ("Investors"); and

WHEREAS, SoCal Holdings, in connection with the bid of the Investors to acquire SoCal, has applied to the FSLIC

pursuant to § 408(e)(1)(B) of the National Housing Act, as amended ("NHA"), 12 U.S.C. § 1730a(e)(1)(B) (1982), and Part 574 of the Regulations for the FSLIC ("Insurance Regulations"), 12 C.F.R. Part 574 (1986), for prior written approval to acquire control of SoCal upon its conversion to the federal stock savings and loan association form through the issuance and sale of all of its common stock to SoCal Holdings ("Application"); and

WHEREAS, Ariadne Australia Limited, a Queensland (Australia) corporation ("Ariadne") and its subsidiaries Federal Broom Company Pty Ltd., an Australian corporation, Napoli Investments Limited, a New Zealand corporation, Brill Limited, a Hong Kong corporation, Raingreen N.V., a Netherlands Antilles corporation and Alapim Holding, B.V., a Netherlands corporation ("Alapim"), pursuant to Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986), have filed with the Federal Home Loan Bank Board ("Bank Board") a rebuttal submission and rebuttal agreement with respect to a rebuttable control determination arising as a result of the ownership of preferred stock of the New Association by Alapim, and the Bank Board has considered the rebuttal submission and rebuttal agreement; and

WHEREAS, Ariadne, the aforementioned subsidiaries and the Investors, pursuant to Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986), have filed with the Bank Board a rebuttal submission and rebuttal affidavits with respect to rebuttable presumptions of concerted action arising from William E. Simon's proposed position as a member of Ariadne's Board of Directors and Ariadne's loan of $5,800,000 to the Investors to acquire, through the Investors' acquisition of SoCal Holdings' common stock, the common stock of the New Association, and the Bank Board has considered the rebuttal submission and Rebuttal affidavits; and

WHEREAS, Roy Doumani, John Harding, Preston Martin and Larry Thrall, as controlling persons, directors, and/or

officers of H.F. Holdings, Inc. ("HFH"), need the approval of the Bank Board under § 408(i)(2)(A) of the NHA 12 U.S.C. § 1730a(i)(2)(A) (1982), and § 584.9(b)(1) of the Regulations for Savings and Loan Holding Companies ("Holding Company Regulations"), 12 C.F.R. § 584.9(b)(1) (1986), to hold positions as officers and/or Directors of SoCal Holdings and the New Association; and

WHEREAS, Roy Doumani, John Harding, Preston Martin and Larry Thrall, as controlling persons, directors, and/or officers of SoCal Holdings, need the approval of the Bank Board under § 408(i)(2)(A) of the NHA, 12 U.S.C. § 1730a(i)(2)(A) (1982), and § 584.9(b)(1) of the Holding Company Regulations, 12 C.F.R. § 584.9(b)(1) (1986), to hold positions as directors and/or officers of HFH and its subsidiary insured institutions after the consummation of the Acquisition; and

WHEREAS, Martin Holdings, Inc., San Francisco, California ("Martin Holdings"), is a savings and loan holding company organized under the laws of the State of Delaware for the purpose of acquiring Preston Martin's shares of common stock of Honolulu Federal Savings and Loan Association, Honolulu, Hawaii ("HonFed"); and

WHEREAS, Martin Holdings, in connection with the bid of the Investors to acquire SoCal, has applied to the FSLIC pursuant to § 408(e)(1)(B) of the NHA, 12 U.S.C. § 1730a(e)(1)(B) (1982), and Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986), for prior written approval to acquire Preston Martin's shares of HonFed common stock; and

WHEREAS, Preston Martin, as a controlling person, director, and officer of Martin Holdings, needs the approval of the Bank Board under § 408(i)(2)(A) of the NHA, 12 U.S.C. § 1730a(i)(2)(A) (1982), and § 584.9(b)(1) of the Holding Company Regulations, 12 C.F.R. § 584.9(b)(1) (1986), to

hold positions as an officer and/or director of SoCal Holdings and the New Association; and

WHEREAS, Preston Martin, as a controlling person, director, and officer of SoCal Holdings, needs the approval of the Bank Board under § 408(i)(2)(A) of the NHA, 12 U.S.C. § 1730a(i)(2)(A) (1982), and § 584.9(b)(1) of the Holding Company Regulations, 12 C.F.R. § 584.9(b)(1) (1986), to hold positions as a director and officer of Martin Holdings after the consummation of the acquisition by Martin Holdings of Preston Martin's shares of HonFed common stock; and

WHEREAS, Martin Holdings has applied the FSLIC pursuant to § 408(g) of the NHA, 12 U.S.C. § 1730a(g) (1982), for prior written approval of its guarantee of Preston Martin's indebtedness to HFH which Mr. Martin incurred in connection with his purchase of shares of HonFed common stock; and

WHEREAS, The board of directors of SoCal, by at least a two-thirds vote of the board, has authorized the conversion of SoCal to the federal stock savings and loan association form and adopted a plan of conversion pursuant to which SoCal will convert to the stock savings and loan association form of organization and will sell its conversion common stock to SoCal Holdings, and, upon the effectiveness of such sale, the present directors of SoCal will resign and be replaced by directors designated by SoCal Holdings and approved by the Bank Board; and

WHEREAS, The Bank Board has considered a proposed "Exchange Agreement" by and between the FSLIC and SoCal, pursuant to which an Income Capital Certificate and a FSLIC promissory note, issued pursuant to a Master Agreement and a Purchase Agreement entered into by and between the FSLIC and SoCal on June 7, 1985, shall be exchanged for one another by the parties and immediately cancelled by their

respective issuers (a copy of which agreement is in the Minute Exhibit File); and

WHEREAS, The Bank Board has considered a proposed "Stock Purchase Agreement" by and between SoCal Holdings and the New Association, pursuant to which SoCal Holdings will acquire all of the common stock of the New Association upon the conversion of SoCal to a federal stock savings and loan association for Six Million Eight Hundred Thousand Dollars ($6,800,000) ("Acquisition") (a copy of which agreement is in the Minute Exhibit File); and

WHEREAS, The Bank Board has considered a proposed "Regulatory Capital Maintenance Agreement" by and among the FSLIC, SoCal Holdings, the Investors and the New Association, pursuant to which SoCal Holdings and the New Association will agree to maintain the regulatory capital of the New Association at a certain level, the Investors will guarantee such agreement to the extent of Five Million Dollars ($5,000,000) and the Investors will grant to the FSLIC certain voting and disposition rights with respect to the common stock of SoCal Holdings held by the Investors (a copy of which agreement is in the Minute Exhibit File); and

WHEREAS, The Bank Board has considered a proposed "Assistance Agreement" by and among the FSLIC, SoCal Holdings and the New Association, pursuant to which the FSLIC will provide certain financial assistance and indemnifications to the New Association and SoCal Holdings to facilitate the Acquisition (a copy of which agreement is in the Minute Exhibit File); and

WHEREAS, The Bank Board has considered the proposed form of a "Common Stock Certificate," which will be issued by the New Association to SoCal Holdings, and the proposed form of the "Preferred Stock Certificates," which will be issued by the New Association to Alapim and FIMA Finance Management, Inc. ("FIMA"), a Panamanian subsidiary of

IFINT, a Luxembourg corporation ("IFINT Sub") (copies of which certificates are in the Minute Exhibit File); and

WHEREAS, The Bank Board has considered memoranda from the Director, Office of the FSLIC, dated April 28, 1987, the Office of Regulatory Policy, Oversight and Supervision dated April 28, 1987, and the Office of the General Counsel dated April 28, 1987, together with accompanying attachments and exhibits (copies of which memoranda are in the Minute Exhibit File):

Supervisory Conversion of SoCal

NOW THEREFORE, IT IS RESOLVED, That on the basis of the administrative record before it, the Bank Board deems and finds that:

(1) SoCal is insolvent, in that its assets are less than its obligations to creditors and others, including its members;

(2) upon the liquidation of SoCal accompanied a pay-ment of insurance of accounts, the members of SoCal would have no realizable equity interest;

(3) pursuant to this resolution, the FSLIC has contracted to provide assistance to the New Association under § 406(f) of the NHA, 12 U.S.C. § 1729(f) (1982); and

(4) following the conversion of SoCal and its acquisition by SoCal Holdings, the New Association would be a viable entity; and

RESOLVED FURTHER, That the conversion of SoCal from the mutual to the stock savings and loan association form of organization, as a part of the supervisory acquisition of SoCal by SoCal Holdings, may be and hereby is approved under § 5(i)(2) of the HOLA, 12 U.S.C. § 1464(i)(2) (1982), and § 402(j) of the NHA, 12 U.S.C. § 1125(j) (1982); and

RESOLVED FURTHER, That upon the conversion of SoCal from the mutual to the stock savings and loan association form, it shall continue to be known is Southern California Federal Savings and Loan Association; and

RESOLVED FURTHER, That pursuant to the findings of this Resolution, good cause exists for a waiver of the requirements of Part 563b of the Insurance Regulations, 12 C.F.R. Part 563b (1980); and

RESOLVED FURTHER, That, pursuant to the exception provisions in §§ 563b.1(a) and 563b.20 of the Insurance Regulations, 12 C.F.R. §§ 563b.1(a) and 563b.20 (1986), the terms of this Resolution, and not the requirements set forth in Part 563b of the Insurance Regulations, 12 C.F.R. § 563b (1986), shall govern the conversion of SoCal from the mutual to the stock savings and loan association form; SoCal shall not be converted in accordance with Subpart C of Part 563b of the Insurance Regulations, 12 C.F.R. Subpart C of Part 563b (1986), and §§ 563b.9 and 10 of the Insurance Regulations, 12 C.F.R. §§ 563b.9 and 10 (1986), shall not apply; and

RESOLVED FURTHER, That without limitation of the immediately preceding paragraph, § 563b.3(i)(3) of the Insurance Regulations, 51 Fed. Reg. 40127, 40149 (1986) (to be codified at 12 C.F.R § 563b.3(i)(3) (1987)), shall not apply to the Acquisition; and

Approval of Acquisition

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, has considered the financial and managerial resources and future prospects of SoCal Holdings and SoCal and the convenience and needs of the communities to be served; and

RESOLVED FURTHER, That, notwithstanding any provision of the law of the State of California, the Bank Board, as operating head of the FSLIC, hereby approves the Acqui-

sition pursuant to § 408(e)(i)(B) of the NHA, 12 U.S.C. § 1730a(e)(1)(B) (1982), and Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986), *provided* that:

1. SoCal shall obtain the approval of its board of directors for the conversion of SoCal from the mutual to the stock savings and loan association form and shall execute an Exchange Agreement, which shall be in the form or substantially in the form presented to the Bank Board, *provided* that the final Form shall be approved by the Office of the General Counsel ("OGC");

2. SoCal Holdings and the New Association shall eachobtain board of directors' approval for consummation of the transactions set forth herein, shall authorize the execution of all documents necessary to consummate such transactions in accordance with all applicable statutory and regulatory requirements and conditions imposed by this Resolution, and shall provide to the OGC satisfactory evidence of such approval and authorization by the respective board of directors;

3. SoCal Holdings and the New Association shall execute an Assistance Agreement, which shall be in the form or substantially in the form presented to the Bank Board, *provided* that the final form shall be approved by the OGC;

4. SoCal Holdings, the Investors and the New Association shall execute as Regulatory Capital Maintenance Agreement, which shall be in the form or substantially in the form presented to the Bank Board, provided that the final form shall be approved by OGC;

5. SoCal Holdings and the New Association shall execute a Dividend Limitation Stipulation, which shall be in the form or substantially in the form presented to the Bank Board, *provided* that the final form shall be approved by OGC;

6. SoCal Holdings and the New Association shall execute a Preferred Stock Redemption Limitation Stipulation, which

shall be in the form or substantially in the form presented to the Bank Board, *provided* that the final form shall be approved by the OGC;

7. SoCal Holdings shall purchase for Six Million Eight Hundred Thousand Dollars ($6,800,000) in cash all of the common stock of the New Association in accordance with the terms of the Stock Purchase Agreement;

8. The New Association shall issue preferred stock with an aggregate par value of Three Hundred Thirty-Three Thousand Two Hundred Fifty Dollars ($333,250), and such stock shall be purchased by Alapim and FIMA for Thirty-Three Million Three Hundred Twenty-Five Thousand Dollars ($33,325,000) ("Preferred Stock Purchase");

9. Promptly after the consummation of the Acquisition, SoCal Holdings shall submit to the FSLIC a copy of the stock certificate issued by the New Association to SoCal Holdings, which certificate shall be in the form of the proposed Common Stock Certificate;

10. Promptly after the consummation of the Preferred Stock Purchase, the New Association shall submit to the FSLIC copies of the stock certificates issued by the New Association to Alapim and FIMA, which certificates shall be in the form of the proposed Preferred Stock Certificates;

11. Promptly after the consummation of the Acquisition, SoCal Holdings shall submit to the Principal Supervisory Agent at the Federal Home Loan Bank of San Francisco ("Principal Supervisory Agent") a letter stating that the purchase of the New Association's common stock by SoCal Holdings was made solely for the purpose of investment and not for resale or distribution, that no material adverse changes have occurred with respect to the business and operations of SoCal Holdings since the date of statements filed with SoCal Holdings' holding company application, except as described in such letter, and that no expense has been incurred by SoCal

Holdings in the acquisition of SoCal that is chargeable to SoCal and that no such expense will be incurred;

12. Not later than 30 days following the effective date of the Acquisition, SoCal Holdings and the Investors shall submit to the Principal Supervisory Agent an opinion of counsel that certifies the effective date of the Acquisition and is to the effect that: all applicable federal and state securities law requirements have been met in connection with the Acquisition; the Acquisition has been duly authorized by the directors of SoCal Holdings and effected in compliance with its charter, bylaws, all applicable laws and regulations, and this Resolution; the Assistance Agreement and the Regulatory Capital Maintenance Agreement have been duly authorized, executed, and delivered, and constitute valid and binding obligations of SoCal Holdings and the Investors; and the transfer by SoCal Holdings to the New Association of cash equal to Six Million Eight Hundred Thousand Dollars ($6,800,000) has been duly authorized by the directors of SoCal Holdings and effected in compliance with its charter, by laws and applicable law;

13. Not later than 30 days following the effective date of the Acquisition, the New Association shall submit to the Principal Supervisory Agent an opinion of counsel that certifies the effective date of the Acquisition and is to the effect that: all applicable federal and state securities law requirements have been met in connection with the Preferred Stock Purchase; the Preferred Stock Purchase has been duly authorized by the directors of the New Association and effected in compliance with the provisions of its charter, bylaws, all applicable laws and regulations, and this Resolution; and the Assistance Agreement and the Regulatory Capital Maintenance Agreement have been duly authorized, executed, and delivered, and constitute valid and binding obligations of the New Association;

14. Not later than 30 days following the effective date of the Acquisition, SoCal Holdings and the Investors shall execute securities certifications precluding securities underwriting and market-making activities by SoCal Holdings and the Investors, which certifications shall be in the forms or substantially in the forms presented to the Bank Board, provided that the final form shall be approved by OGC;

15. Not later than 30 days following the effective date of the Acquisition, SoCal Holdings and the Investors shall execute a misconduct certification stating, among other things, that they have not been the subject of any criminal, civil or administrative judgments, consents or orders, which certification shall be in the form or substantially in the form presented to the Bank Board, *provided* that the final form shall be approved by the OGC;

16. SoCal Holdings and the New Association shall execute a Stipulation Concerning Directors and Officers of the New Association, which shall be in the form or substantially in the form presented to the Bank Board, *provided* that the final form shall be approved by the OGC, and which shall provide for the following:

(a) With in 4 months following the date of the stipulation, the New Association shall have submitted evidence that the institution's Board of Directors will include at least twelve members and that no more than five of which may be salaried officers/employees of the institution, or its subsidiaries/affiliates, or directors of its subsidiaries/affiliates;

(b) Within 15 days following the date of the stipulation, SoCal Holdings and the New Association shall have:

(1) Submitted evidence to the Supervisory Agent that the board of directors has established an audit committee and an investment committee, the membership of which must be comprised to board members, with no director serving on both committees, *provided, however*, that one director may

serve on both committees for a period of no more than 30 days from the date of the stipulation. Further, a majority of the committee membership must consist of directors who are not salaried officers/employees of the association or its subsidiaries/affiliates. The audit committee shall function pursuant to the guidelines of FHLBB Memorandum R 44 and the primary responsibilities of the investment committee shall include interest rate risk management, credit risk management, and asset/liability management. Both committees shall submit formal written reports to the association's Board of Directors, at least quarterly, with copies of such reports being sent to the Principal Supervisory Agent for a period of 5 years beginning with the end of the first quarter following commencement of operations; and

(2) Submitted to the Supervisory Agent for ap-proval the names of the Chief Executive Officer, Chief Financial Officer and Chief Lending Officer, who are qualified, experienced, and capable of managing the operations of the institution. The performance of such individuals will be periodically reviewed and their continued employment will be subject to the Principal Supervisory Agent's approval for a period of 3 years. Provided further, that said individuals shall be subject to termination of employment if the Principal Supervisory Agent takes supervisory objection to their continued employment. Provided finally, that in the event of a change of control of the institution within 3 years of the date of the stipulation, such 3 year period shall recommence in its entirety; and

(c) Any officer, director or 10 percent stockholder of the insured institution or any subsidiary of the insured institution who is also engaged in the business of real estate development, building or construction, may not secure financing for such business from the insured institution;

17. The New Association shall adhere to the provisions of the Operating Plan dated April 1, 1987 as submitted in

conjunction with the Application; the New Association shall have 90 days from the effective date of the Acquisition to submit revisions or modifications to the Operating Plan, any revisions or modifications of which shall be subject to approval by the Supervisory Agent at the Federal Home Loan Bank of San Francisco ("Supervisory Agent"); any changes in, or deviation from, the Operating Plan as submitted shall require prior written approval of the Supervisory Agent during the five-year period following the effective date of the Acquisition; and the Board of Directors of the New Association shall be responsible for review of the Operating Plan on an annual basis to assure the New Association's adherence to the plan and will report to the Supervisory Agent on an annual basis as to its findings;

18. The New Association shall submit on a monthly basis to the Supervisory Agent a report, acceptable to the Supervisory Agent, detailing the 30, 60 and 90 day delinquencies for each category of lending and an additional schedule detailing the activity in the New Association's real estate owned;

19. Not later than 60 days following the date of this Resolution, Arbur, Inc. shall submit Forms 660 satisfactory to the Supervisory Agent with respect to the following persons: William E. Simon, Jr., John Peter Simon, Mary Beth Simon Streep, Carol Leigh Simon Porges, Aimee Simon, Julie Ann Simon and Johanna Katherine Simon;

20. Martin Holdings must execute a securities stipulation in the form executed by SoCal Holdings with 30 days of the Bank Board's approval of the Acquisition; and

21. Martin Holdings must execute within 30 days of such approval a regulatory capital maintenance agreement stating that if Martin Holdings at any time acquires more than 25 percent of the outstanding HonFed com-mon stock, Martin Holdings will maintain the regulatory capital of Honfed at the

levels required by Bank Board Resolution 86-910, and will contribute capital, in a form satisfactory to the Supervisory Agent, to remedy any shortfall in proportion to its ownership of HonFed common stock; and

RESOLVED FURTHER, That SoCal Holdings and the New Association shall submit to the Principal Supervisory Agent an independent certified public accountant's opinion that each has accounted for the Acquisition in accordance with generally accepted accounting principles ("GAAP") or in accordance with GAAP as it may be modified by the following procedures, which shall be employed:

(a) Push-down accounting shall be used to reflect the Acquisition on the books of the New Association;

(b) The cash contribution by the FSLIC to the New Association, pursuant to the Assistance Agreement, may be deemed a contribution to the regulatory capital and may be booked as a direct credit to the New Association's regulatory capital; and

(c) The value of any intangible assets resulting from the Acquisition shall be amortized by the New Association over a period not to exceed 25 years by the straight line method.

RESOLVED FURTHER, That not later than 90 days following the effective date of the Acquisition, SoCal Holdings and the New Association each shall furnish an analysis accompanied by a concurring opinion from independent public accountants, satisfactory to the Principal Supervisory Agent, which shall (a) specifically describe, as of the effective date of the Acquisition, any intangible assets, including goodwill, or the discounts of assets arising from the Acquisition to be recorded on SoCal Holdings's or the New Association's books for purposes of separate and consolidated financial statements; and (b) substantiate the reasonableness and conformity with regulatory requirements of the amounts attributable to intangible assets, including goodwill, and the dis-

counts of assets and the related amortization periods and methods; and

RESOLVED FURTHER, That pursuant to the findings of this Resolution, good cause exists for a waiver of the requirements of Part 563g of the Insurance Regulations applicable to the Acquisition and the Preferred Stock Purchase and the same are hereby waived pursuant to § 563g.14(a)(2) of the Insurance Regulations; and

Holding Company Approval

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, has considered the financial and managerial resources and future prospects of SoCal Holdings and the New Association; and

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, finds that the Acquisition satisfies the approval standards of § 408(e)(1)(B) of the NHA, 12 U.S.C. § 1730a(e)(1)(B) (1982), and Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986); and

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, hereby approves the acquisition of control of the New Association by SoCal Holdings pursuant to § 408(e)(1)(B) of the NHA, 12 U.S.C. § 1730a(e)(1)(B) (1982), and Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986), subject to the aforementioned conditions; and

RESOLVED FURTHER, That the Bank Board hereby accepts the submission of Ariadne and its subsidiaries with respect to rebuttal of control of the New Association and hereby authorizes the Secretary or Assistant Secretary to sign the rebuttal agreement submitted therewith on behalf of the Bank Board; and

RESOLVED FURTHER, That the Bank Board hereby accepts the submission of Ariadne and its subsidiaries and the

Investors with respect to the rebuttal of presumptions of concerted action and hereby authorizes the Secretary or Assistant Secretary to sign the affidavits submitted therewith on behalf of the Bank Board; and

RESOLVED FURTHER, That the Bank Board finds that it is consistent with the public interest that Roy Doumani, John Harding, Preston Martin and Larry Thrall, as controlling persons, directors and/or officers of HFH hold simultaneously positions as directors and/or officers of SoCal Holdings or the New Association, and hereby approves such interlocks pursuant to § 408(i)(2)(A) of the NHA, 12 U.S.C. § 1730a(i)(2)(A) (1982), and § 584.9(b)(1) of the Holding Company Regulations, 12 C.F.R. § 584.9(b)(1) (1986); and

RESOLVED FURTHER, That the Bank Board finds that it is consistent with the public interest that Roy Doumani, John Harding, Preston Martin and Larry Thrall, as controlling persons, directors and/or officers of SoCal Holdings, hold simultaneously positions as directors and/or officers of HFH or its subsidiary insured institutions, and hereby approves such interlocks pursuant to §408(i)(2)(A) of the NHA, 12 U.S.C. § 1730a(i)(2)(A) (1982), and § 584.9(b)(1) of the Holding Company Regulations, 12 C.F.R. § 584.9(b)(1) (1986); and

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, has considered the financial and managerial resources and future prospects of Martin Holdings and HonFed; and

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, finds that the acquisition by Martin Holdings of Preston Martin's shares of HonFed common stock satisfies the approval standards of § 408(e)(1)(B) of the NHA, 12 U.S.C. § 1730a(e)(1)(B) (1982), and Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986); and

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, hereby approves the acquisition of Preston Martin's shares of HonFed common stock by Martin Holdings pursuant to § 408(e)(1)(B) of the NHA, 12 U.S.C. § 1730a(e)(1)(B) (1982), and Part 574 of the Insurance Regulations, 12 C.F.R. Part 574 (1986), subject to the afore-mentioned conditions; and

RESOLVED FURTHER, That the Bank Board finds that it is consistent with the public interest that Preston Martin, as a controlling person, director and officer of Martin Holdings, hold simultaneously positions as a director or officer of SoCal Holdings or the New Association, and hereby approves such interlock pursuant to § 408(i)(2)(A) of the NHA, 12 U.S.C. § 1730a(i)(2)(A) (1982), and § 584.9(B)(1) of the Holding Company Regulations, 12 C.F.R. § 584.9(b)(1) (1986); and

RESOLVED FURTHER, The Bank Board finds that it is consistent with the public interest that Preston Martin, as a controlling person, director and officer of SoCal Holdings, hold simultaneously positions as a director and officer of Martin Holdings, and hereby approves such interlock pursuant to § 408(i)(2)(A) of the NHA, 12 U.S.C. § 1730a(i)(2)(A) (1982), and § 584.9(b)(1) of the Holding Company Regulations, 12 C.F.R. § 584.9(b)(1) (1986); and

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, hereby approves Martin Holdings' guarantee of Preston Martin's indebtedness to HFH, which Mr. Martin incurred in connection with his purchase of shares of HonFed common stock, pursuant to § 408(g) of the NHA, 12 U.S.C. § 1730a(g) (1982); and

Grounds for Financial Assistance

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, hereby determines, pursuant to § 406(f)(1)- (4) of the NHA, 12 U.S.C. § 1729(f)(1)-(4) (1982), that (1) financial assistance by the FSLIC is necessary

to prevent the default of SoCal and to facilitate the acquisition of SoCal by SoCal Holdings; and (2) the amount of such assistance, to be provided in accordance with the terms and conditions of the proposed assistance agreement, would not exceed that amount reasonably necessary to save the cost of liquidating, including paying the insured accounts of, SoCal; and

RESOLVED FURTHER, That the proposed Assistance Agreement is hereby approved, and the Director or Deputy Director, Office of the FSLIC, Director, Financial Assistance Division, Office of the FSLIC, or the designee of any of them ("Director"), is hereby authorized to execute on behalf of the FSLIC an agreement in the form or substantially in the form of the proposed Assistance Agreement, provided that the final form of such agreement has been approved by the OGC; and

RESOLVED FURTHER, That the Director is authorized to take such further actions as may be necessary or appropriate to exercise the rights and fulfill the obligations of the FSLIC contained in the Assistance Agreement; and

Approval of Certificates

RESOLVED FURTHER, That the proposed forms of the Preferred Stock Certificates and Common Stock Certificate are hereby approved, provided that the final forms of such certificates shall be approved by the OGC; and

Marketing and Acquisition Findings

RESOLVED FURTHER, That the Bank Board, as operating head of the FSLIC, hereby determines with respect to the Acquisition, that:

(1) Severe financial conditions exist which threaten the stability of SoCal, the accounts of which are insured by the FSLIC;

(2) Severe financial conditions exist which threaten the stability of a significant number of institutions,

the accounts of which are insured by the FSLIC ("Insured institutions"), and of insured institutions possessing significant financial resources;

(3) SoCal is a failing institution that is eligible for assistance pursuant to § 406(f) of the NHA, 12 U.S.C. § 1729(f) (1982), in connection with the Acquisition;

(4) The procedures used by agents of the FSLIC with respect to SoCal to solicit practicable offers from prospective purchasers or merger partners qualified and capable of acquiring the failing institution's assets and liabilities comply with the standards employed by the FSLIC in marketing failing institutions;

(5) The Bank Board, in making the findings and issuing the approvals contained in this Resolution, has given full and due consideration to minimizing the cost of financial assistance and the maintenance of specialized depository institutions;

(6) The acquisition of SoCal by SoCal Holdings will lessen the risk to the FSLIC;

(7) Offers for SoCal were solicited from qualified thrift institutions, bank holding companies, and investors located in or outside of California;

(8) Only one bid to acquire SoCal was offered in addition to the Investors' bid and the cost of the other bid exceeded the cost of liquidating SoCal; and

(9) The offer of the Investors to acquire SoCal presents the least risk to the FSLIC of any proposal submitted for SoCal; and

Issuance of Forms

RESOLVED FURTHER, That all forms issued by the New Association after completion of the conversion evidencing funds on deposit with the New Association shall be in the form approved by the Principal Supervisory Agent and shall indicate that the New Association is a stock savings and loan association; and

Issuance of Charter and Bylaws

RESOLVED FURTHER, That a Charter in the form of the proposed Federal Stock Charter, which allows for removal of directors with or without cause, a copy of which form is in the Minute Exhibit File, is hereby approved and shall be issued to the New Association, and the Secretary or an Assistant Secretary may attest and date the Charter upon the direction of the OGC, and such Charter shall be deemed issued at the time of such dating and attesting by the Secretary or Assistant Secretary; and

RESOLVED FURTHER, That the Bylaws of the New Association in the form proposed, which allow for removal of directors with or without cause, a copy of which form is in the Minute Exhibit File, are hereby approved; and

Insurance of Accounts and Membership in the Federal Home Loan Bank

RESOLVED FURTHER, That all accounts in the New Association shall continue to be insured by the FSLIC to the same extent that they were insured prior to the conversion of SoCal to the federal stock savings and loan association form, and the New Association shall continue its membership in the Federal Home Loan Bank of San Francisco; and

Employment Contracts

RESOLVED FURTHER, That pursuant to 563.39 of the Insurance Regulations, 12 C.F.R. § 563.39 (1986), all obligations of SoCal under employment contracts of SoCal are

hereby terminated by the FSLIC, effective as of the effective date of the Acquisition; and

Prevention of Probable Failure

RESOLVED FURTHER, That the Bank Board finds that approval of the Acquisition, and the related acquisition of Preston Martin's shares of HonFed common stock by Martin Holdings, pursuant to § 408(e)(1)(B) of the NHA, 12 U.S.C. § 1729a(e)(1)(B) (1982), are necessary to prevent the probable failure of SoCal; and

Supervisory Acquisition

RESOLVED FURTHER, That the Bank Board finds that the Acquisition is instituted for supervisory reasons; and

Forbearances

RESOLVED FURTHER, That the Secretary or an Assistant Secretary is authorized and directed to send to the New Association a letter concerning supervisory forbearance by the Bank Board and the FSLIC with respect to certain regulatory requirements, in the Form or substantially in the form of the letter in the Minute Exhibit File, provided that the final form of such letter shall be approved by the OGC; and

Tax Certification

RESOLVED FURTHER, That the Bank Board finds and certifies that the ground set forth in § 5(d)(6)(A)(i) of the HOLA, as amended, 12 U.S.C. § 1464(d)(6)(A)(i) (1982), exists with respect to SoCal in that SoCal is insolvent; and that the record before the Bank Board contains nothing to show or from which it could be inferred that SoCal had intentionally placed itself in the position of being insolvent for the purpose of obtaining any tax advantages pursuant to 26 U.S.C. § 368(a)(3)(D) (1982); and

RESOLVED FURTHER, That the Secretary or an Assistant Secretary is hereby authorized and directed to issue to SoCal

Holdings a letter with respect to SoCal certifying on behalf of the Bank Board the matters set forth in the immediately preceding resolving paragraph, and the Secretary or an Assistant Secretary is hereby authorized to provide a copy of such letter to any agency of the United States upon request; and

Effective Date of Conversion and Acquisition

RESOLVED FURTHER, That the supervisory conversion of SoCal shall be effective as of the full execution of the Exchange Agreement, and the Acquisition shall be effective as of 11:59 p.m. on the effective date of the Stock Purchase Agreement.

By the Federal Home Loan Bank Board

Jeff Sconyers
Secretary

FEDERAL HOME LOAN BANK BOARD

Pursuit of Claims of
Southern California Federal Savings
and Loan Association,
Beverly Hills, California

No. 87-512
Date: April 30, 1987

WHEREAS, The Federal Home Loan Bank Board has authorized the supervisory conversion of Southern California Federal Savings and Loan Association, Beverly Hills, California, a federal mutual savings and loan association ("Association"), into a federal stock savings and loan association, pursuant to Resolution No. 87-511, dated April 30, 1987; and

WHEREAS, Certain claims of the Association against certain parties will be transferred to the Federal Savings and Loan Insurance Corporation ("FSLIC"), and certain potential claims of the Association against certain parties may be transferred to the FSLIC, pursuant to the proposed Assistance Agreement (a copy of which is in the Minute Exhibit File);

NOW, THEREFORE, IT IS RESOLVED, That the Director or Deputy Director, Office of the FSLIC, Director, Financial Assistance Division, Office of the FSLIC, or the designee of any of them, is hereby authorized to take whatever actions are deemed appropriate, including litigation, to recover on such claims of the Association from any such parties, provided that the Office of the General Counsel shall concur in any such action.

By the Federal Home Loan Bank Board

Jeff Sconyers
Secretary

FEDERAL HOME LOAN BANK BOARD

Implementation Resolution

No. 87-513

Date: April 30, 1987

WHEREAS, The Director or Deputy Director, Office of the Federal Savings and Loan Insurance Corporation ("FSLIC"), or the Director, Financial Assistance Division, Office of the FSLIC, or the designee of any of them ("Director"), has been authorized by Federal Home Loan Bank Board ("Bank Board") Resolutions No. 87-511 and 87-513, dated April 30, 1987, to execute on behalf of the FSLIC, in its corporate capacity, an Assistance Agreement ("Assistance Agreement") with SoCal Holdings, Inc., San Francisco, California, a state-chartered savings and loan holding company ("SoCal Holdings"), and Southern California Federal Savings and Loan Association, Beverly Hills, California, a federal stock savings and loan association ("New Association"), a Regulatory Capital Maintenance Agreement ("Regulatory Capital Maintenance Agreement") with SoCal Holdings, the New Association and certain investors in SoCal Holdings and other documents, and to pursue certain claims; and

WHEREAS, The Assistance Agreement, the Regulatory Capital Maintenance Agreement and other documents impose certain rights, duties, and obligations upon the FSLIC, and permit the pursuit of such claims, that do not require basic determinations of policy; and

WHEREAS, In the administration of the Assistance Agreement, the Regulatory Capital Maintenance Agreement, and of any rights or obligations of the FSLIC under them, and in the pursuit of such claims, it may be necessary or desirable that the FSLIC contract for legal, auditing, or other services or that the FSLIC authorize the settlement of certain claims:

NOW THEREFORE, IT IS RESOLVED, That the Bank Board, as operating head of the FSLIC, finds that expen-

ditures of the FSLIC pursuant to and in administration of the Assistance Agreement, the Regulatory Capital Maintenance Agreement, and in pursuit of such claims, are necessary, nonadministrative, and made under the National Housing Act, as amended ("NHA"), and shall be incurred, allowed, and paid under the provisions of the fourth sentence of § 402(c)(5) of the NHA, 12 U.S.C. § 1725(c)(5) (1982), without regard to the provisions of any other law governing the expenditure of public funds; and

RESOLVED FURTHER, That, effective upon the execution of the Assistance Agreement and the Regulatory Capital Maintenance Agreement, the Director is hereby authorized and directed to take such actions as may be desirable or necessary to fulfill the rights, duties, and obligations of the FSLIC in its corporate capacity under the Assistance Agreement, the Regulatory Capital Maintenance Agreement and other authorized documents, and in the pursuit of such claims, and to incur, allow, and pay all expenditures in fulfillment of such rights, duties, and obligations, pursuant to the fourth sentence of § 402(c)(5) of the NHA, 12 U.S.C. § 1725(c)(5) (1982), including, but not limited to:

(1) The payment of any and all amounts required by the Assistance Agreement or the Regulatory Capital Maintenance Agreement;

(2) Contracting for legal, accounting, or other services relating to the implementation of the Assistance Agreement, the Regulatory Capital Maintenance Agreement and other documents, and in the pursuit of such claims, *provided* that the form of any such contract shall be approved by the Office of the General Counsel ("OGC");

(3) The assignment, pursuit, and settlement of claims, *provided* that the form of any assignment or settlement agreement entered into by the FSLIC shall be approved by the OGC;

(4) The administration of any asset or claim acquired pursuant to the Assistance Agreement or the Regulatory Capital Maintenance Agreement, *provided* that any contract pertaining to such asset or claim, and the satisfaction, settlement, or termination of any such claim, shall be approved by the OGC; and

(5) The waiver, if deemed necessary or desirable by the Director, of provisions of the Assistance Agreement or the Regulatory Capital Maintenance Agreement concerning filings, representations, warranties, or certifications by the New Association, *provided* that the form of any waiver by the FSLIC shall be approved by the OGC; and

RESOLVED FURTHER, That the OGC may also exercise the authority conferred by the preceding paragraphs with respect to contracting on behalf of the FSLIC for legal or other related services needed to implement the Assistance Agreement and the Regulatory Capital Maintenance Agreement and the pursuit of such claims; and

RESOLVED FURTHER, That the Director is authorized and directed to take all other actions necessary and appropriate to exercise the rights and fulfill the duties and obligations of the FSLIC in the administration of the Assistance Agreement and the Regulatory Capital Maintenance Agreement.

By the Federal Home Loan Bank Board

Jeff Sconyers
Secretary

FEDERAL HOME LOAN BANK BOARD

Approval of the Acquisition of Southern California Federal Savings and Loan Association, Beverly Hills, California, by SoCal Holdings, Inc., San Francisco, California

No. 87-514
Date: April 30, 1987

RESOLVED, That the acquisition of all of the common stock of Southern California Federal Savings and Loan Association, Beverly Hills, California, a federal stock savings and loan association ("New Association"), by SoCal Holdings, Inc., San Francisco, California ("SoCal Holdings"), pursuant to a Stock Purchase Agreement by and between SoCal Holdings and the New Association ("Stock Purchase Agreement"), is hereby approved, effective as of the effective date of the Stock Purchase Agreement, and subject to any conditions that may be imposed by the Federal Home Loan Bank Board in any concurrent resolution or action issued as of the date of this Resolution.

By the Federal Home Loan Bank Board

Jeff Sconyers
Secretary

[JX 1426]

Federal Home Loan Bank Board

May 27, 1987

Preston Martin
Chairman of the Board and
Chief Executive Office of
SoCal Holdings, Inc.
One Montgomery Street, West Tower
San Francisco, California 94101

Re: The Supervisory Conversion and Acquisition
of Southern California S&A, A FS&LA
Beverly Hills, California
FHLBB No. 8258)
by
SoCal Holdings, Inc.
San Francisco, California
(FHLBB No. H-1112)

Dear Mr. Martin:

Concurrent with the approval of the above-captioned transaction, the following forbearances are granted:

1. The assets acquired by Southern California FS&LA, Beverly Hills, California ("SoCal Federal") from Southern California S&LA, a FS&LA, Beverly Hills, California ("Southern California") will be deemed to have been acquired in an acquisition instituted for supervisory reasons. Therefore, pursuant to any section of the regulations administered by the Federal Home Loan Bank Board where scheduled items are referred to as "assets acquired in an acquisition instituted for supervisory reason", scheduled items attributable to Southern California shall be excluded from the computation of scheduled items in determining whether SoCal Federal meets the requirements of such sections following the effective acquisition date.

2. Not later than 60 days following the effective date of the acquisition, SoCal Federal shall submit to the Supervisory Agent an independent certified public accountant's opinion that SoCal Federal has accounted for the acquisition in accordance with generally accepted accounting principles ("GAAP"), or in accordance with GAAP except to the extent that the following may depart from GAAP and which is hereby approved by the Board for purposes of regulatory reporting by SoCal Federal to the Board: (a) the cash contribution by FSLIC to SoCal Federal with respect to Southern California pursuant to the Assistance agreement shall be deemed a contribution to regulatory net worth, and may be booked as a direct credit to SoCal Federal, (b) the value of any unidentifiable intangible assets resulting from accounting for the acquisition in accordance with the purchase method may be amortized by SoCal Federal over a period not to exceed 25 years by the straight line method.

The forbearance or waivers extended by this letter do not relieve SoCal Federal of its continuing obligations to maintain records of its reserve and net worth condition and to report its financial condition in accordance with applicable regulatory requirements. This letter does not and shall not be construed to constitute forbearance or waiver by the Bank Board or the Corporation with respect to any regulatory or other requirements other than those encompassed within the preceding paragraphs 1 and 2. Other than the actions to enforce the regulatory requirements waived in accordance with paragraphs 1 and 2 and the statutory provisions authorizing imposition of the waived requirements, insofar as such requirements are waived, the Bank Board and the Federal Savings and Loan Insurance Corporation expressly reserve all of their statutory rights and power with respect to SoCal Federal including, without limitation, those under Section 5

of the Home Owners' Loan Act of 1933 and Sections 406 and 407 of the National Housing Act.

By the Federal Home Loan Bank Board

Jeff Sconyers
Secretary

(4)

Supreme Court, U.S.
FILED
MAY 24 2006
OFFICE OF THE CLERK

No. 05-1221

In the Supreme Court of the United States

PRESTON MARTIN, ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether, under the terms of the Regulatory Capital Maintenance Contract at issue in this case, petitioners were entitled to damages for dilution of their ownership interest in a thrift and a thrift holding company after Congress enacted legislation phasing out the thrift's reliance upon goodwill to satisfy regulatory capital requirements.

TABLE OF CONTENTS

Page

Opinions below 1
Jurisdiction 1
Statement 2
Argument 12
Conclusion 29

TABLE OF AUTHORITIES

Cases:

Bluebonnet Sav. Bank, FSB v. *United States*, 266 F.3d 1348 (Fed. Cir. 2001) 20, 22

Charles River Bridge v. *Warren Bridge*, 36 U.S. (11 Pet.) 420 (1837) 25

Coast Fed. Bank, FSB v. *United States*, 323 F.3d 1035 (Fed. Cir. 2003) 3

Domino's Pizza, Inc. v. *McDonald*, 126 S. Ct. 1246 (2006) 28

Home Sav. of Am., FSB v. *United States:*
51 Fed. Cl. 487 (2002) 27
399 F.3d 1341 (Fed. Cir. 2005) 27

Keefe v. *Clark*, 322 U.S. 393 (1944) 25

La Van v. *United States*, 382 F.3d 1340 (Fed. Cir. 2004) 20, 21, 28

Massie v. *United States*, 166 F.3d 1184 (Fed. Cir. 1999) 23

National R.R. Passenger Corp. v. *Atchison, Topeka, & Santa Fe Ry.*, 470 U.S. 451 (1985) 24, 25

United States v. *Winstar Corp.*, 518 U.S. 839 (1996) 2, 7, 25

Case—Continued: Page

Wisniewski v. *United States*, 353 U.S. 901 (1957) 20, 26

Statute:

Financial Institutions Reform, Recovery, and Enforcement Act, Pub. L. No. 101-73, 103 Stat. 183 .. 2

In the Supreme Court of the United States

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PRESTON MARTIN, ET AL., PETITIONERS

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UNITED STATES OF AMERICA, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-30a) is reported at 422 F.3d 1319. The opinion of the Court of Federal Claims on damages (Pet. App. 31a-124a) is reported at 57 Fed. Cl. 598. The opinion of the Court of Federal Claims on liability (Pet. App. 125a-175a) is reported at 52 Fed. Cl. 531.

JURISDICTION

The corrected judgment of the court of appeals was entered on August 30, 2005. Petitions for rehearing were denied on December 27, 2005 (Pet. App. 176a-177a). The petition for a writ of certiorari was filed on March 21, 2006. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. This is one of approximately 30 (out of an original total of approximately 122) *Winstar*-related cases (see *United States* v. *Winstar Corp.*, 518 U.S. 839 (1996)) that were filed after the enactment of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA), Pub. L. No. 101-73, 103 Stat. 183, and that remain pending in the Court of Appeals for the Federal Circuit or the Court of Federal Claims. In this case, the court of appeals affirmed the trial court's ruling that the government had breached a contract with a thrift holding company and the thrift institution it owns, and the court affirmed in part and reversed in part the trial court's award of damages to those parties. The court of appeals, however, reversed the trial court's holding that the government had breached a broad contract with petitioners that encompassed several distinct documents, and it also held that petitioners were not entitled to damages under a narrower contract theory.

2. This case involves a group of shareholders, including Roy Doumani, Preston Martin, Larry B. Thrall, William E. Simon, Jr., and a Simon family-owned corporation, Arbur, Inc. In 1987, those investors and others formed a holding company, SoCal Holdings, Inc. (SCH), which later acquired a failed thrift and renamed it Southern California Federal Savings and Loan Association (SoCal). Pet. App. 5a.

The Federal Home Loan Bank Board (FHLBB), a federal agency that regulated the thrift industry, approved the acquisition. Pet. App. 131a. The Federal Savings and Loan Insurance Corporation (FSLIC), an entity subordinate to the FHLBB, infused $217.5 million into SoCal; permitted SoCal not to reduce its goodwill by the $217.5 million infusion (the "capital credit"), as

would have been required by Generally Accepted Accounting Principles (GAAP); permitted SoCal to record almost $300 million in goodwill on its balance sheet; and authorized SoCal to amortize the goodwill over a 25-year period. *Id.* at 131-133a. See *Coast Fed. Bank, FSB* v. *United States*, 323 F.3d 1035 (Fed. Cir. 2003) (en banc) (discussing relationship between capital credit and goodwill).

Various aspects of the transaction were memorialized in various documents, executed by different parties. They included: (1) an Assistance Agreement, signed by FSLIC, SCH, and SoCal, but *not* by petitioners; (2) FHLBB resolutions which, among other things, authorized the transmittal of a Forbearance Letter from FHLBB to SCH; and (3) a Regulatory Capital Maintenance Agreement (RCMA), signed by FSLIC, SCH, SoCal, and each of petitioners.

Assistance Agreement. The Assistance Agreement was signed by FSLIC, SCH, and SoCal, but not by petitioners. Under the Assistance Agreement, the government agreed, *inter alia*, that "[f]or purposes of reports to the Bank Board, the [capital credit] shall be credited to [SoCal's] regulatory capital account and shall constitute regulatory capital." C.A. App. A400755.[1] The As-

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[1] The relevant provision states in full:

> For purposes of reports to the Bank Board, the cash contribution made under § 3(a)(1) above [which required FSLIC to wire $217.5 million to SoCal] shall be credited to [SoCal's] regulatory capital account and shall constitute regulatory capital as defined in § 561.13 of the Insurance Regulations, 51 Fed. Reg. 33,565 (1986) (to be codified at 12 C.F.R. § 561.13 (1987)), notwithstanding the accounting treatment of such contribution that must be reflected in any filing that [SoCal] may make, whether

sistance Agreement contained an "Entire Agreement" clause, which stated:

> This Agreement, together with any interpretation or understanding agreed to in writing by the parties, constitutes the entire agreement between the parties and supersedes all prior agreements and understandings of the parties in connection with it, excepting only any resolutions or letters concerning the Conversion, the Acquisition or this Agreement issued by [FHLBB] or [FSLIC] in connection with the approval of the Conversion, the Acquisition, and this Agreement.

Pet. App. at 131a.

The Assistance Agreement also contained a "Sole Benefit" clause, which stated that all conditions, obligations, and responsibilities under the agreement were "for the sole benefit of the parties hereto and for the benefit of no other person," and that nothing in the agreement was "intended or shall be construed to give any person other than the parties hereto any legal or equitable right, remedy, or claim under, or in respect to, this Agreement or any of its provisions." Pet. App. 11a.

FHLBB Resolutions. The Bank Board adopted resolutions which, among other things, authorized the transmittal of a Forbearance Letter from FHLBB to SCH. The Forbearance Letter, in turn, authorized SoCal to depart from GAAP by counting the $217.5 million cash infusion as a contribution to SoCal's regulatory net worth. It also authorized SoCal to amortize an addi-

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to the Bank Board or otherwise, that requires the submission of financial statements prepared in accordance with GAAP.

C.A. App. A400755.

tional $79 million in goodwill for a period of 25 years by the straight-line method for purposes of calculating SoCal's regulatory capital. See Pet. App. 5a, 130a, 133a.

Regulatory Capital Maintenance Agreement. In addition to FSLIC, SCH, and SoCal, petitioners too signed the RCMA. Pet. App. 180a-196a. It had the following key provisions:

Section 1 of the RCMA required SCH and SoCal to maintain SoCal's compliance with certain federal capital requirements, "*provided* * * * that" the capital credit be "includable in capital for purposes of" determining whether those capital requirements are satisfied.[2] Pet. App. 182a. Section 1 itself did not mention petitioners.

Section 2 of the RCMA stated that "[f]or purposes of this Agreement, any computation of [SoCal's] Required Regulatory Capital shall be as determined" by the Principal Supervisory Agent of the Bank Board (P.S.A.) "in accordance with," *inter alia*, the "includable in capital"

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[2] Section 1 of the RCMA is reproduced in full at Pet. App. 181a-183a. In relevant part, it states:

> [SCH] and [SoCal] shall cause the 'regulatory capital,' as defined in [certain regulations], or any successor regulation, as now or hereafter in effect, of [SoCal] to be maintained at the level required by [other regulations], or any successor regulation, as now or hereafter in effect ("Regulatory Capital Regulation") ("Required Regulatory Capital"), * * * *provided* that [the regulations regarding certain liabilities and "base ratio" shall be calculated in a certain way], and *provided further*, that regardless of any changes in the method of calculating regulatory capital or the items includable in such calculation, the $217.5 million of assistance from [FSLIC] shall be includable in capital for purposes of determining whether [SoCal] has maintained its regulatory capital at the Required Regulatory Capital level.

proviso in Section 1 and "shall reflect," *inter alia*, that proviso. Pet. App. 182a-183a.[3]

Section 4 of the RCMA, which did mention petitioners, stated that "so long as [SCH] shall be obligated pursuant to § 1, [petitioners] * * * hereby guarantee the performance of [SCH] and [SoCal] under § 1, *provided* that [certain guarantees of petitioners shall be joint and several], and *provided further*, that the personal obligations of [petitioners] under said guarantees shall not exceed $5,000,000 in the aggregate." Pet. App. 183a.

The RCMA thus required petitioners to contribute up to $5 million, if necessary, to enable SoCal to maintain its capital at acceptable levels under federal capital requirements. But SoCal's obligation to do so under the RCMA (and, therefore, petitioners' obligation as guarantors) was conditioned on the government's permitting SoCal to include the $217.5 million FSLIC contribution as capital in determining, for purposes of the RCMA, whether SoCal satisfied the specified regulatory capital requirements. The RCMA also required petitioners to maintain control of SCH. Pet. App. 185a. The RCMA did not mention goodwill or the method that was to be utilized to account for goodwill. See *id.* at 180a-196a.

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[3] Section 2 of the RCMA is reproduced in full at Pet. App. 183a. In relevant part, it states:

> For purposes of this Agreement, any computation of [SoCal's] Required Regulatory Capital shall be as determined by the P.S.A., in accordance with applicable regulations, standards and procedures generally applicable to institutions under the P.S.A.'s jurisdiction and the second proviso of § 1, and shall reflect any directives issued by the P.S.A., in accordance with such regulations, standards and procedures and the second proviso of § 1, regarding [SoCal's] calculation of Required Regulatory Capital.

3. In August 1989, Congress enacted FIRREA to address widespread problems in the savings and loan industry. FIRREA and its implementing regulations phased out reliance upon goodwill and other intangible assets as regulatory net worth over a five-year period. See *Winstar*, 518 U.S. at 856-857. To the extent that SoCal had relied upon goodwill (including the capital credit) to meet its capital requirements, the phase-out required SoCal to obtain more money to replace the phased-out goodwill.

In 1992, SCH raised $48 million by selling notes to two new investors and to Arbur. Pet. App. 6a. As part of the transaction, SCH converted its original common shares, owned by petitioners, to Class B common shares, and issued new Class A common stock to the two new investors and Arbur. *Id.* at 7a. The result of the recapitalization was to reduce petitioners' ownership of SCH from 100% to 51.36%. *Ibid.* SCH infused $43.5 million of the proceeds into SoCal and, as a result, SoCal returned to regulatory capital compliance. *Id.* at 6a-7a, 62a.

SoCal's financial condition, however, continued to deteriorate. In 1995, SCH raised $60.5 million in new debt and preferred stock from the 1992 investors, $60.4 million of which SCH then infused into SoCal. Pet. App. 7a, 66a, 68a. As part of that capital-raising transaction, SCH cancelled its outstanding Class B common stock, which was owned by petitioners. *Id.* at 7a, 67a.

4. In 1993, SoCal, SCH, and petitioners filed a complaint in the Court of Federal Claims, alleging that the government had entered into a contract permitting SoCal to include the $21.7.5 million capital credit and an additional $79 million in supervisory goodwill in its calculation of its regulatory capital. Pet. App. 127a, 140a.

The complaint alleged that Congress had breached that contract through the enactment of FIRREA. *Id.* at 127a. In response, the government acknowledged that the Assistance Agreement was an express contract between FSLIC and SoCal and SCH permitting SoCal to include the $217.5 million capital credit in its regulatory capital. The government denied, however, that petitioners had standing to enforce that promise, because they were not parties to the Assistance Agreement. See *id.* at 8a.

The Court of Federal Claims granted the plaintiffs' motions for summary judgment on liability. With respect to petitioners, the court concluded that the Assistance Agreement's Entire Agreement clause incorporated the RCMA and the FHLBB resolutions authorizing the transmittal of the Forbearance Letter which, in turn, authorized the inclusion of goodwill (including the capital credit) in the calculation of SoCal's regulatory capital. Pet. App. 146a. The trial court further held that the Entire Agreement clause rendered "unenforceable" the Assistance Agreement's Sole Benefit clause, to the extent the latter clause would exclude petitioners as parties. *Id.* at 145a. The court concluded that, although petitioners had not signed and were not parties to the Assistance Agreement itself, they were parties to what the court characterized as an "overall" agreement that encompassed the terms of the Assistance Agreement, the RCMA, and the FHLBB resolutions/Forbearance Letter adopted in connection with the transaction. *Id.* at 146a, 149a.

After a trial on damages, the trial court awarded over $90 million to petitioners based upon a "dilution theory." The court accepted that, in the absence of the breach, the 1992 and 1995 recapitalizations would not

have occurred, and petitioners would have continued to possess their shares. The court therefore held that petitioners are entitled to the value of the shares they would have possessed in 1998. Pet. App. 106a-111a, 123a. The court also awarded $65.4 million in damages to SCH and SoCal. *Id.* at 123a.

5. On appeal, the Federal Circuit affirmed in part and reversed in part the trial court's award of damages to SCH and SoCal. Pet. App. 22a-27a. No party has sought further review of that decision. In the ruling at issue here, the court of appeals reversed the award of damages to petitioners. *Id.* at 27a.

The court held that the trial court had erred in concluding that the government had entered into an "overall" contract to which petitioners were parties, with the government's promises regarding the treatment of capital credits and supervisory goodwill running to all of the parties, thereby according standing to petitioners to recover damages for a breach. Pet. App. 10a-19a. The court of appeals found that conclusion to be contrary to the plain terms of the Assistance Agreement, to which SCH and SoCal were parties, but petitioners, as shareholders of SCH, were not. *Id.* at 11a-14a. The court noted in particular that the Sole Benefit clause of the Assistance Agreement excludes non-parties, such as petitioners, from the benefits of the Assistance Agreement, and that the trial court's conclusion to the contrary concededly made the Sole Benefit clause "unenforceable." *Id.* at 12a; see *id.* at 146a.

The court of appeals further held that the trial court had erred in concluding that the Entire Agreement clause required that petitioners be accorded the benefits of the Assistance Agreement notwithstanding their express exclusion under the terms of the Sole Benefit

clause. The court noted that the Entire Agreement clause of the Assistance Agreement by its terms incorporated the FHLBB resolutions, the Forbearance Letter, and other "interpretations or understandings agreed to in writing by the parties." Pet. App. 13a. The court held, however, that the RCMA was not one of the types of documents incorporated into the Assistance Agreement, because it was neither an FHLBB resolution nor an "interpretation[] or understanding[] agreed to in writing by the parties" to the Assistance Agreement. *Ibid.* Rather, the court explained, the RCMA "is a separate contract that involves additional parties and distinct promises, including its own Entire Agreement clause." *Ibid.* Thus, the court concluded, "the plain language of the Sole Benefit clause and the Entire Agreement clause evidences the parties' intent to limit the scope of the Assistance Agreement to its specified terms." *Ibid.*

The court of appeals noted that the trial court had relied upon petitioners' participation, as shareholders, in the conversion and acquisition process to hold that the petitioners were parties to an "overall" contract based on the Assistance Agreement. Pet. App. 15a. The court explained, however, that petitioners' participation in the process does not show that they became parties to the Assistance Agreement or a broader, "overall" agreement, because of the well-settled principle "that a corporation is generally considered to be a separate legal entity from its shareholders." *Ibid.* Under the Assistance Agreement, the law of California was to govern its construction, and the court explained that California law would plainly treat the corporations as separate entities from their shareholders in the circumstances of this case. *Id.* at 15a-16a. In short, "[h]aving chosen to limit

their personal liability by adopting a corporate form" with all of its advantages of limited liability, petitioners could not "rely on their involvement in the negotiation process or their role in funding a transaction to alter their chosen legal status" and be treated as the real contracting parties when it suited their interests. *Id.* at 17a.

The Federal Circuit then considered whether the much more limited RCMA, to which petitioners *were* parties, entitled petitioners to recover damages. Pet. App. 19a-22a. The court noted that the trial court itself did not find that petitioners' status as signatories to the RCMA was sufficient to allow them to recover damages. *Id.* at 15a n.4. In analyzing the RCMA, the court of appeals noted that the RCMA contained references to the capital credit (but not to goodwill). *Id.* at 19a-20a. Assuming, but not deciding, that the government had breached the RCMA, *id.* at 20a, the court determined that petitioners were not entitled to damages for dilution of their ownership interest in SCH and SoCal, because petitioners' relinquishment of their equity was neither caused by, nor a foreseeable result of, any alleged breach of the RCMA. *Id.* at 20a-21a.

Judge Mayer dissented in part. Pet. App. 28a-30a. He would have affirmed the trial court's conclusion that "[t]he combined content of the [RCMA], the Assistance Agreement, and the [FHLBB] implementing resolutions * * * proves that [petitioners] entered into an overall contract with the government." *Id.* at 28a. In his view, that "overall contract" gave petitioners "standing to enforce both the capital credit and the supervisory goodwill promises of the government." *Id.* at 30a. Judge Mayer did not disagree with the court's conclusion that

petitioners had no right to damages based upon a breach of the narrower RCMA itself.

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or of any other court of appeals. The narrow issues decided by the court of appeals concerning the construction of the particular documents in this case and the causation and foreseeability of petitioners' alleged damages by the alleged breach do not warrant further review.

1. Petitioners do not challenge the court of appeals' conclusion that the trial court erred in finding a broad, overall agreement based on the Assistance Agreement, incorporating the FHLBB Resolutions and Forbearance Letter, and including the RCMA as well. Nor do petitioners challenge the court of appeals' articulation, see Pet. App. 20a-21a, of the general rules governing contract damages under an expectation, reliance, or restitution theory, including the court's recitation of the ordinary causation and foreseeability requirements for expectation damages. See Pet. 20. Petitioners' sole challenge is to the application of those general standards to the particular contract and the particular transaction in this case. Further review of that fact-based claim is not warranted. In any event, the court of appeals correctly held that petitioners are not entitled to damages for breach of the RCMA.

a. The plain terms of the RCMA make clear that it did not include a promise by the government to permit SoCal to include the $217.5 million capital credit in its regulatory capital for federal regulatory purposes. Without such a promise, petitioners' claim for damages must be rejected.

As discussed above, Section 1 of the RCMA by its terms embodied a promise by SCH and SoCal that they would "cause" SoCal to satisfy what Secton 1 termed the "Required Regulatory Capital" level, *i.e.*, the level required by federal regulations. Pet. App. 181a-182a. Section 1 then stated two qualifications on that promise by SCH and SoCal, each introduced with a "provided that" clause. *Id.* at 182a. Under the second "provided that" clause, SCH and SoCal would cause SoCal to satisfy the Required Regulatory Capital level, "*provided further* that * * * the $217.5 million of assistance from the CORPORATION [*i.e.*, the so-called "capital credit"] shall be includable in capital for purposes of determining whether [SoCal] has maintained its regulatory capital at the Required Regulatory Capital level." *Ibid.*; see note 2, *supra*. Accordingly, SCH and SoCal would have an obligation under the RCMA to ensure compliance with the Required Regulatory Capital level *provided that* the $217.5 million cash infusion was includable in capital for purposes of the calculation. Because the government's commitment regarding the capital credit was introduced in a "provided that" clause, it was merely a condition on the performance of SCH and SoCal. The language of Section 1—which was written as a condition on the perofrmance by SCH and SoCal, not as an affirmative undertaking by FSLIC—thus makes clear that the government was not making a more general, affirmative commitment in the RCMA about how SoCal's capital would be calculated or regulated for other purposes. While such a more general commitment was made to SCH and SoCal (but *not* to petitioners) in the Assistance Agreement, see pp. 14-15, *infra*, it was not included in the RCMA.

Section 2 reinforced that conclusion. Under Section 2, "[f]or purposes of this Agreement, any computation of [SoCal's] Required Regulatory Capital shall be as determined by," *inter alia*, "the second proviso of § 1," *i.e.*, the $217.5 million "includable in capital" proviso. Pet. App. 182a-183a. Section 2 thus made clear that the $217.5 million "includable in capital" proviso was to be controlling solely "[f]or purposes of this Agreement," *i.e.*, for purposes of determining whether SCH and SoCal would have to perform their contractual commitment in the RCMA to maintain SoCal's capital at a certain level. The proviso was to have no further force in, for example, calculating SoCal's compliance with regulatory or statutory capital standards for thrifts more generally, or the liability of the government for breach of any promises FSLIC may have made to SCH or SoCal in some other agreement.

The above promises made by SCH and SoCal in Section 1 of the RCMA are relevant to petitioners solely by virtue of Section 4 of the RCMA. Section 4 states that, "so long as [SCH] shall be obligated pursuant to § 1," petitioners "guarantee the performance of [SCH] and [SoCal] under § 1," subject to petitioners' maximum obligation in the aggregate of $5 million. Pet. App. 183a. Because *SCH and SoCal* have contractual obligations under Section 1 to maintain capital levels only if the $217.5 million "includable in capital" proviso in that section is satisfied, Section 4 similarly limits *petitioners'* obligations as guarantors of SCH and SoCal to circumstances in which the $217.5 million "includable in capital" proviso is satisfied. Neither Section 4 nor any other portion of the RCMA, however, includes or suggests a government promise to SCH or SoCal, much less to petitioners, to permit SoCal to treat the capital credit in any

particular way for purposes other than determining the obligations of SCH and SoCal—and the derivative obligations of petitioners as guarantors of the performance of SCH and SoCal—under Section 1 of the RCMA.

To be sure, a more general promise committing the government to calculate SoCal's capital in a particular way for federal regulatory purposes was made in the Assistance Agreement, to which petitioners were not parties. The terms of that promise may usefully be contrasted with the RCMA. Under the Assistance Agreement, the government agreed that "[f]or purposes of reports to the Bank Board, the [capital credit] shall be credited to [SoCal's] regulatory capital account and shall constitute regulatory capital." C.A. App. A400755; see note 1, *supra*. Had the parties desired in the RCMA to include an affirmative promise by the government to permit the capital credit to constitute regulatory capital generally under the applicable federal regulations, the parties thus had a readily available model to achieve that end. The RCMA, however, was directed to a different and more limited purpose—*i.e.*, establishing the obligation of SCH and SoCal, as corporations, to maintain the regulatory capital of SoCal, subject to certain conditions. And the purpose of Section 4 of the RCMA was also different and far more limited still—to obtain the personal guarantee of petitioners, as individual shareholders of SCH, for the performance by SCH and SoCal of their conditional obligations under Section 1. Furthermore, even that guarantee was capped at $5 million. Accordingly, petitioners did not obtain—and the government did not agree to—a general contractual commitment *to petitioners* that the capital credit would constitute regulatory capital of SoCal for purposes of deter-

mining compliance with federal banking regulations.[4] Indeed, it is exceedingly unlikely that the government would have exposed itself to the sort of broad liability petitioners assert in this case in exchange for a conditional guarantee capped at $5 million.

b. With the terms of the RCMA in mind, petitioners' damages claim can be analyzed. The court of appeals correctly rejected petitioners' claim "that the incorporation of the capital credit promise into the terms of the RCMA is sufficient to uphold the Court of Federal Claims' award of damages." Pet. App. 20a. Because the treatment of the capital credit was only a condition on petitioners' performance of *their* obligation, there was no breach of the RCMA by the government when the condition that excused Sch and SoCal from performing occurred.

Put another way, as the court of appeals explained, "the damages for which [petitioners] seek to recover, namely the dilution and the extinguishment of their ownership interest in SCH, were not caused by the obli-

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[4] In the court of appeals, petitioners and the government focused almost all of their attention on whether there was an overall agreement to which petitioners were parties and which included not only the RCMA, but also the Assistance Agreement, the Bank Board Resolutions, and the Forbearance Letter. Only three pages in one of the two 59-page appellate briefs submitted by the two separate groups of petitioners mentioned the possibility of an asserted breach of the RCMA as a separate basis for liability. See C.A. Br. for Roy Doumani et al. 19-22. The parties' focus on the Assistance Agreement and Forbearance Letter is entirely explicable when the terms of the RCMA are examined, since those terms make clear that the RCMA did not include a general promise, as in the Assistance Agreement, that the capital credit "shall be credited to [SoCal's] regulatory capital account and shall constitute regulatory capital" for federal regulatory purposes. C.A. App. A400755.

gations they incurred in the RCMA." Pet. App. 20a. Indeed, as the court of appeals further noted, "[t]he RCMA did not require that the Individual Plaintiffs invest in SCH," but "[a]t the most, the RCMA obligated the Individual Plaintiffs to collectively contribute to SCH and SoCal an additional $5 million in the event that SCH and SoCal did not maintain SoCal's regulatory capital at the required level." *Ibid.* And petitioners in fact never even made that contribution. *Ibid.* Thus, because the government's only undertaking to petitioners in the RCMA was a "provided that" condition on petitioners' performance of their up-to-$5 million guarantee (which was in turn conditional on a failure by SCH and SoCal to fulfill their conditional undertakings as primary obligors under Section 1 of the RCMA)—and because petitioners never rendered that performance—the nonoccurrence of the condition that excused SCH and SoCal from their obligations under the RCMA could not have caused petitioners any damages under the RCMA, much less the damages they claimed for dilution of their ownership interest in SCH.

That holding was independently sufficient to dispose of petitioners' claims. Nonetheless, the court of appeals additionally went on to address the issue in terms of foreseeability and damages, concluding that, "even if [the court] assume[s] that the passage of FIRREA constituted a breach of the RCMA, [petitioners] are not entitled to recover the damages they seek." Pet. App. 20a. The damages petitioners seek are for dilution of their ownership interest in SCH and SoCal. From the beginning, however, petitioners (like all other shareholders of thrifts and holding companies) faced a risk that if the thrift needed more capital, SCH might issue more stock (and even cancel the old stock) to raise

money to infuse into the thrift. That risk would have existed even if the shareholders never entered into the RCMA. Thus, assuming there was a breach here, petitioners could prevail only if the RCMA shifted that particular risk—the risk that SCH would dilute petitioners' ownership interest in order to raise capital—from the shareholders to the government.

As noted above, the RCMA was directed to petitioners' obligation to invest *additional* funds in SCH, and the assurances petitioners sought regarding the conditions that would have to exist in order for that obligation to be triggered. Nothing in the RCMA addressed the more general risk that petitioners' pre-existing stock in SCH and SoCal would be diluted. As the court of appeals explained,"there are no terms in the RCMA that require [petitioners] to raise capital for SCH and SoCal by diluting their ownership interest in order to issue equity to new investors," but, "[a]t the most, the RCMA obligates [petitioners] to contribute an additional $5 million to the operation of SCH and SoCal." Pet. App. 21a. Accordingly, from the standpoint of the RCMA, a claim that petitioners lost a $5 million contribution required by the RCMA might have stated a claim for foreseeable damages up to that amount in certain circumstances, had petitioners ever made such a contribution. But a claim that petitioners' pre-existing stock was diluted was not within the scope of risks addressed by the RCMA, and any dilution of petitioners' stock was accordingly not foreseeable with respect to the RCMA. Accordingly, even if it is assumed, *arguendo*, that the change in regulatory capital requirements after FIRREA could be regarded as a breach of the RCMA, "[b]ased on the unambiguous terms of the RCMA, [petitioners'] loss of their ownership interests was neither

the foreseeable result of nor caused by the government's breach of the RCMA and therefore dilution damages cannot be awarded as a form of expectation damages." *Ibid.*

c. Petitioners argue that further review is warranted on the ground that the court of appeals minted a new, and unduly limited, rule of contract damages in this case. They contend that, "[a]lthough [the court of appeals] *recited* the usual foreseeability standard, the court rejected expectation damages as a matter of law by adding a novel limitation to that standard: that the contract itself must require the equity loss upon breach or the acquisition of the destroyed property in the first place." Pet. 16; see Pet. 19-20.

Petitioners are correct that the court of appeals recited the ordinary standards of causation and foreseeability for contract damages. But they err in asserting that the court otherwise added any "novel limitation" to those standards. Contrary to petitioners' contentions, the court of appeals never stated any general principle that expectation damages are awardable only if the contract "require[s] the equity loss upon breach" or if the contract requires "the acquisition of the destroyed property in the first place." Pet. 16. Rather, the court applied the general principles of causation and foreseeability to this particular contract, where the only possible deficiency was the alleged failure of a condition precedent to petitioners' own obligations. In those circumstances, any claim for damages by petitioners would have to flow from their performance of their own obligations; having negotiated a contract in which the government's obligation was merely a condition precedent to theirs, they cannot now obtain consequential damages

based on the proposition that the government made a general and unqualified promise.

Petitioners also argue (Pet. 21) that "the Federal Circuit nowhere questioned as a *factual* matter the trial-court finding that the loss of the 1987 equity was a foreseeable consequence of the Government's breach of its regulatory-capital contract." The trial court considered the RCMA, however, only as part of a broad, "overall" contract, a contract whose existence the court of appeals correctly rejected. See Pet. App. 10a-19a. Thus, the trial court never considered whether the petitioners' relinquishment of their equity was foreseeable as a result of an asserted breach of the RCMA standing alone. See *id.* at 15a n.4 ("It is noteworthy that the Court of Federal Claims did not find that the status of [petitioners] as signatories to the RCMA was sufficient to allow them to recover damages."). In any event, in light of the terms of the RCMA, no such finding would have been possible.

d. Finally, petitioners argue (Pet. 22-24) that the court of appeals' decision conflicts with its prior decisions in *Bluebonnet Savings Bank, FSB* v. *United States*, 266 F.3d 1348 (Fed. Cir. 2001), and *La Van* v. *United States*, 382 F.3d 1340 (Fed. Cir. 2004). Further review is not warranted to address a claim of an intra-circuit conflict. *Wisniewski* v. *United States*, 353 U.S. 901, 902 (1957) (per curiam). In any event, there is no such conflict.

In *Bluebonnet*, the shareholder obligated himself to infuse money into the thrift at specified intervals. Based upon the facts of that case, the trial court held, and the Federal Circuit affirmed, that it was foreseeable that a breach of the promises in a forbearance letter sent to the shareholder would interfere with the shareholder's

ability to raise capital. 266 F.3d at 1354. The damages sought in *Bluebonnet* arose from the alleged increased costs to the shareholder of making the required infusions after the breach. The alleged breach of the RCMA in this case arose in a completely different factual environment. Unlike in *Bluebonnet*, the contract in this case contained only a condition precedent to petitioners' performance, not an unqualified promise by the government. Moreover, unlike in *Bluebonnet*, the shareholders here did not actually infuse money into the thrift pursuant to the contract.

In the "fact-specific dispute" before the Federal Circuit in *La Van*, 382 F.3d at 1342, the trial court held that "the Government contracted with the Acquirors for * * * the amortization of the goodwill resulting from the [*Winstar*-type] transaction over thirty-five years." *Id.* at 1345. The court of appeals affirmed that conclusion. By contrast, the government entered into no such agreement with petitioners in the RCMA.[5] And just as in *La Van* the court of appeals held that "the standard for damages was the usual make-whole principle based on foreseeability," Pet. 24 (citing *La Van*, 382 F.3d at 1350-1351), the court of appeals in this case correctly held that "[e]xpectation damages are recoverable provided

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[5] Moreover, contrary to petitioners' assertion (Pet. 24), the court of appeals did not hold that the plaintiffs in LaVan were entitled to "expectation damages * * * for loss in value of their stock." Rather, the court noted the trial court's unappealed award of restitution for "the amount of the [plaintiffs'] initial investment," 382 F.3d at 1349, and held that "the trial court erred in denying [plaintiffs] the opportunity to present a case for expectancy damages," *id.* at 1350 (emphasis added). The court declined to decide whether the plaintiffs were entitled to expectation damages, instead "remand[ing] for the trial court to determine whether expectancy damages would be appropriate in the present case." *Ibid.*

they are actually foreseen or reasonably foreseeable, are caused by the breach of the promisor, and are proved with reasonable certainty." Pet. App. 20a-21a (quoting *Bluebonnet*, 266 F.3d at 1355).

2. Petitioners also argue (Pet. i, 27) that review should be granted to determine whether the Bank Board resolutions themselves "created contract rights for petitioners."

a. Initially, petitioners never argued to the court of appeals that the Bank Board resolutions themselves created contract rights, and the court of appeals never addressed that issue. Instead, prior to the petition for certiorari, petitioners contended that the FHLBB resolutions had been incorporated into the Assistance Agreement and that those resolutions—and, in particular, the Forbearance Letter to which they referred—created contractual rights on that basis. The court of appeals agreed that "[t]he Entire Agreement clause [in the Assistance Agreement] specifically incorporates * * * resolutions or letters from the FHLBB or the FSLIC." Pet. App. 13a. But the court held that the petitioners were not parties to the Assistance Agreement into which the resolutions had been incorporated—a holding that petitioners do not challenge. *Ibid.* The contention presented in the petition, that the resolutions alone created a contract with petitioners, is thus a new contention that this Court should not consider.

b. In any event, further review would not be warranted to address petitioner's highly case-specific contention that the Bank Board resolutions in this case created contractual rights in petitioners. By statute and regulation, petitioners needed various approvals by the Bank Board before they could consummate the transaction in which they acquired SoCal. Three Bank Board

resolutions granted those approvals. Resolution No. 87-514 approved the acquisition of SoCal's common stock by SCH, subject to any conditions that were imposed in a concurrent resolution. Pet. App. 223a. Resolution No. 87-511 noted the statutory and regulatory requirements for FHLBB approval of the conversion of SoCal to a stock organization, the acquisition of SoCal's stock by SCH, and the occupation of certain corporate offices by petitioners. *Id.* at 200a-201a. The resolution granted the requisite approvals subject to certain conditions, including (1) the execution of the Assistance Agreement by SoCal and SCH; (2) the execution of the RCMA by SoCal, SCH, and petitioners; (3) the execution of a Dividend Stipulation by SoCal and SCH; and (4) other stipulations and documents. *Id.* at 201a. The resolution also authorized the transmittal of the Forbearance Letter. *Id.* at 217a. The third resolution, No. 87-513, authorized FSLIC to execute and implement the Assistance Agreement, the RCMA, and other documents. *Id.* at 220a.

As petitioners acknowledge, "the requirements for a contract with the Government" include "mutual intent to contract." Pet. 29 (quoting *Massie* v. *United States*, 166 F.3d 1184, 1188 (Fed. Cir. 1999)). The Bank Board resolutions evidence no such mutual intent; they do not state that the Bank Board "agrees," "contracts," or "promises" to do anything. The resolutions are framed as exercises of federal regulatory authority, not contracts binding the government (and petitioners) and requiring payment of damages by the government (or petitioners) upon "breach" of the resolutions. Although the resolutions refer in various places to documents that are undoubtedly contractual (*i.e.*, the Assistance Agreement and the Regulatory Capital Maintenance Agreement), the resolutions do not incorporate those agreements; to

the contrary, the Resolutions distinguish between those contracts, which are referred to as "agreements," and other documents, which are termed "stipulations." See, *e.g.*, Pet. App. 207a. Moreover, the documents in this case were carefully structured so that one agreement (the Assistance Agreement) imposed obligations upon SCH and SoCal but not on petitioners, while another agreement (the RCMA) included petitioners. Having structured the transaction to take advantage of the separate identities of SoCal and SCH and the limited liability advantage offered by those separate identities, petitioners cannot now frustrate that structure by claiming that, by virtue of the Bank Board resolutions, the parties' efforts to distinguish between the corporations (SCH and SoCal) and petitioners as individuals who were shareholders of SCH, and to limit petitioners' obligations and rights, were entirely illusory.

To adopt petitioners' view that a request for and grant of regulatory approval forms a contract between the regulatory agency and regulated entity would conflict with long-settled principles of administrative law. As this Court explained in addressing an analogous situation in *National Railroad Passenger Corp.* v. *Atchison, Topeka & Santa Fe Railway*, 470 U.S. 451 (1985), "absent 'an adequate expression of an actual intent' of the State to bind itself, this Court simply will not lightly construe that which is undoubtedly a scheme of public regulation to be, in addition, a private contract to which the State is a party." *Id.* at 466-467 (citation omitted). *National Railroad Passenger Corp.* involved a claim that a statute, rather than a regulatory action, constituted a contract between the government and private entities. But the underlying rule in both instances is that "the principal function of a legislature [or regula-

tory agency] is not to make contracts, but to make laws that establish the policy of the state." *Id.* at 466. "Policies, unlike contracts, are inherently subject to revision and repeal, and to construe laws [or regulatory actions] as contracts when the obligation is not clearly and unequivocally expressed would be to limit drastically the essential powers of a legislative [or administrative] body." *Ibid.* To imply a contractual undertaking from a regulatory approval is impermissible, because in this case, as in *National Railroad Passenger Corp.*, "[t]he continued existence of a government would be of no great value, if, by implications and presumptions, it was disarmed of the powers necessary to accomplish the ends of its creation." *Keefe* v. *Clark*, 322 U.S. 393, 397 (1944) (quoting *Charles River Bridge* v. *Warren Bridge*, 36 U.S. (11 Pet.) 420, 548 (1837)).

c. Contrary to petitioners' contention (Pet. 28), the decision below does not conflict with this Court's decision in *Winstar*. In *Winstar*, the plurality first concluded that an FHLBB resolution had been incorporated into the Supervisory Action Agreement (whose status as a contractual document was undisputed) by means of an integration clause. 518 U.S. at 862-863 (opinion of Souter, J). That conclusion was sufficient to establish that the terms of the contract were supplemented by the FHLBB resolution; the court of appeals in this case rejected the analogous conclusion with respect to the RCMA, and petitioners do not challenge that holding. Petitioners rely, however, on the plurality's added statement that "[t]o the extent that the integration clause leaves any ambiguity, the other courts that construed the documents found that the realities of the transaction favored reading those documents as contractual commit-

ments, not mere statements of policy, and we see no reason to disagree." *Id.* at 863 (citation omitted).

That alternative reasoning by the plurality, which was not addressed by the concurring Justices, was not necessary to the decision in *Winstar*. By its own terms, moreover, that reasoning is inapplicable here, because "the other courts" that construed the documents here did not find that they were contractual commitments; to the contrary, neither lower court expressly addressed whether the Bank Board resolutions alone were sufficient to form a contract. In any event, the facts of this case are fundamentally different from those in *Winstar*. Here, the parties plainly did provide in a contract (the Assistance Agreement) for the regulatory treatment of goodwill, and they also made quite clear that that agreement incorporated certain Bank Board resolutions. But, unlike in *Winstar*, the parties also decided not to include petitioners in that agreement. What petitioners seek in this case, unlike in *Winstar*, is to use the Bank Board resolutions to create additional contract rights for themselves, notwithstanding the fact that, at the time of contracting, the parties decided to grant those rights only to others.

d. Petitioners also argue (Pet. 28-29) that the decision of the court of appeals conflicts with other decisions of the Federal Circuit. Further review would not be warranted to address a claim of an intra-circuit conflict. *Wisniewski*, 353 U.S. at 902. Moreover, the court of appeals' decision could not conflict on this point with any of its prior decisions, because the court of appeals in this case did not address (because petitioners did not raise) the argument that the Bank Board resolutions alone constituted contracts between the government and petitioners.

In any event, even had the court of appeals held that the Bank Board resolutions were not contractual documents giving rights to petitioners, there would have been no intra-circuit conflict. Petitioners cite *Home Savings of America, FSB* v. *United States*, 399 F.3d 1341 (Fed. Cir. 2005). In *Home Savings*, the court of appeals held that although a parent company, Ahmanson, was not a party to the Assistance Agreements in that case, it was a party to overall contracts with the government pursuant to which its subsidiary, Home Savings, acquired several thrifts. *Id.* at 1349. Unlike in this case, the Bank Board resolutions in *Home Savings* conditioned approval of the transaction on a direct undertaking by Ahmanson to assume full financial responsibility for the thrift. See, *e.g.*, *Home Sav. of Am., FSB* v. *United States*, 51 Fed. Cl. 487, 498 (2002); see also 399 F.3d at 1349 (Bank Board resolutions memorialized "reciprocal promises that were part of the overall bargains between the plaintiffs and the government"). In this case, by contrast, the Bank Board resolution approving SCH's acquisition of SoCal mentions petitioners, see Pet. App. 197a-199a, but it does not impose direct obligations on them or condition approval of the acquisition upon reciprocal promises by them.

Petitioners also cite *La Van*. See Pet. 29. The court of appeals in this case specifically distinguished *La Van*, noting that "the shareholders [in *La Van*] were so critical to the conversion transaction that they, rather than the corporation, were essentially the direct purchasers of the converted federally-insured institution." Pet. App. 17a. The court also noted that the contractual documents in *La Van* had not identified the state law intended to govern the contracts in that case, and the court in *La Van* accordingly had no occasion to consider

the legal requirements under a particular state's law "mandating a distinction between a corporation and its shareholders." *Id.* at 18a; cf. *Domino's Pizza, Inc.* v. *McDonald*, 126 S. Ct. 1246 (2006) (emphasizing importance of distinction between corporation and its shareholders). In this case, by contrast, the parties provided in the Assistance Agreement that California law would govern the contract, and the court of appeals' analysis emphasized that under California law "there is no justification" to "disregard * * * the corporate structure invoked by [petitioners] facilitating the acquisition and conversion of [SoCal]." Pet. App. 17a. Finally, the court of appeals in *La Van* relied on specific evidence that the government intended to contract with the shareholders separately from the corporation in which they owned shares, such as internal deliberations, 382 F.3d at 1348, and an internal memorandum stating that "arm's length" negotiations were being conducted with the shareholder plaintiffs, *id.* at 1343. Here, in contrast, the facts show that any intent to reach an agreement with petitioners was confined to the terms contained in the RCMA.

In any event, the extent to which particular Bank Board resolutions constituted contracts between the thrift regulators, the banks, and their shareholders in the course of the 1980s is confined to the *Winstar* context. Only 30, out of the original total of approximately 122, *Winstar*-related cases are still pending. The question presented concerning the precise circumstances under which Bank Board regulations during the 1980s did—or did not—attain contractual status is one of limited future importance.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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IN THE

Supreme Court of the United States

PRESTON MARTIN, ROY DOUMANI, BEVERLY W. THRALL (Successor to the Claims of Larry B. Thrall), ARBUR, INC., WILLIAM E. SIMON, JR., J. PETER SIMON, AND GEORGE J. GILLESPIE, III (Executors of the Estate of William E. Simon, Sr.),

Petitioners,

v.

UNITED STATES, *et al.*,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

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RULE 29.6 STATEMENT

There has been no change since the petition. *See* Pet. ii.

TABLE OF CONTENTS

	Page
RULE 29.6 STATEMENT	i
TABLE OF AUTHORITIES	iv
A. The First Question Warrants Review	2
B. The Second Question Warrants Review	8
CONCLUSION	10

TABLE OF AUTHORITIES

CASES — Page

Bluebonnet Sav. Bk. v. United States, 266 F.3d 1348 (Fed. Cir. 2001) 7
Cardinal Chem. Co. v. Morton Intern., Inc., 508 U.S. 83 (1993) 7
East River S.S. Corp. v. Transamerica Delaval, Inc., 476 U.S. 858 (1986) 5
Home Savings of America v. United States, 399 F.3d 1341 (Fed. Cir. 2005) 9, 10
La Van v. United States, 382 F.3d 1340 (Fed. Cir. 2004) 7, 9, 10
National Railroad Passenger Corp. v. Atchison, Topeka & Santa Fe Ry., 470 U.S. 451 (1985) ... 8
United States v. Winstar Corp., 518 U.S. 839 (1996) 3, 9

OTHER AUTHORITIES

E. Farnsworth, *Contracts* (1982) 5
R. Lord, *Williston on Contracts* (4th ed.) 5
Restatement (Second) of Contracts (1979)
§ 2 ..... 3, 9
§ 3 ..... 3, 9
§ 4 ..... 3, 9
§ 202 ..... 3, 9
§§ 224-230 6
§ 305 4
§ 344 5
§ 347 5
Petition for Certiorari, in *United States v. IBM Corp.*, 517 U.S. 843 (1996), 1995 WL 17013668 7

REPLY BRIEF FOR PETITIONERS

The principal question presented is whether, when a party to a Government contract suffers a breach that causes factually foreseeable expectation damages (as the Federal Circuit accepted here). federal contract law nevertheless bars such damages unless the contract specifically provides for them. The Federal Circuit held that it does, engrafting a radical limitation, unsupported in any authority, on the entitlement to expectation damages. Because of the Federal Circuit's unique role in government contract law, its deviation from well-established standards and its own prior decisions on so fundamental an issue will cause serious harm until corrected.

The Government cannot defend the court's holding. It primarily seeks to avoid the issue by disputing the Federal Circuit's own (correct) premise that the Government breached its contract with petitioners. When the Government does discuss the actual ruling, it makes a simple and decisive error. It treats contract provisions that limit promisees' express obligations, and thus protect against their downside risk, as if they legally implied curtailment of their entitlement to the benefit of their bargain (their expected upside potential). That confusion of contract obligations with contract opportunities, aside from being illogical and unaccompanied by a single citation of authority, flouts the defining feature of contract damages—the guarantee of the "benefit of the bargain." The Federal Circuit's damages ruling is plainly wrong and should be reviewed and reversed.

The question whether the Board resolutions themselves created contract rights also warrants review. The Government is wrong in saying that petitioners failed to preserve this issue. On the merits, the Government has neither authority nor analysis to deny that financial-transaction-approving resolutions like the ones here create contract rights. Other Federal Circuit decisions plainly recognize such resolutions' enforceability as contracts, creating a conflict that warrants review.

A. The First Question Warrants Review

The Government incorrectly asserts that the petition's first question, about contract damages law, merely contests the application of settled law. Opp. 12. The Federal Circuit did not hold that, on the facts, petitioners failed to meet the accepted standard of factually foreseeable expectation damages; it did not even conduct a clear-error review of the trial court's factual finding of foreseeability (and *could not* have reversed that finding as a factual matter, as Pet. 21-22 explains). Rather, the court held that expectation damages could not, as a matter of law, include the breach-caused destruction of petitioners' property (their 1987 equity) simply because petitioners' *obligations* in the breached contract (the RCMA) did not include surrender (or initial acquisition) of that property. That is a legal ruling, and it is insupportable; indeed, its novelty is shown by the fact that the Government's entire argument on the merits (Opp. 12-20) is devoid of any citation to legal authority, whether precedent or the *Restatement*'s governing principles.[1]

1. The Government's main argument relies on what it recognizes was *not* the ground of the Federal Circuit's decision: a contention that the RCMA did not include a capital-credit promise by the Government. Opp. 12-16. The Federal Circuit, however, at least accepted (as the Government agrees), and is better read as having affirmatively concluded, that the Government breached the RCMA when it altered the regulatory treatment of capital credits. Pet. App. 19a ("Recital G and § 1 [of the RCMA] include the government's promise that SCH and SoCal will be able to account for $217.5 million in capital credits as part of its regulatory capital."); *id.* at 20a ("the incorporation of the capital credit

[1] The Government misstates the amount at stake: it says that "the trial court awarded over $90 million to petitioners" (Opp. 8), when the award to petitioners was just over $28 million (App. 123a; *see* Pet. 11).

promise into the terms of the RCMA"). The Federal Circuit thus adopted a legal rule that limits damages for a breach, and it is that rule, which the Government struggles to explain and support (*see* pages 4-7, *infra*), that contract parties and courts now must follow.

The Federal Circuit was correct in declining to adopt the Government's argument that the RCMA contains no capital-credit promise. RCMA § 1 in terms says: "regardless of any changes in the method of calculating regulatory capital or the items includable in such calculation, the $217.5 million of assistance from the CORPORATION [Government] shall be includable in capital for purposes of determining whether the NEW ASSOCIATION [SoCal] has maintained its regulatory capital" at the 3% level § 1 requires. Pet. App. 182a. RCMA § 4 requires *petitioners* (the "ACQUIRING GROUP") to guarantee that level and also to maintain their equity ownership, and RCMA §§ 5 and 7 require *petitioners* to forfeit their stock in certain circumstances if their equity or the capital level falls too much. Pet. App. 183a. The recitals preceding those provisions, moreover, not only state that the Government "has agreed" to the capital-credit regulatory treatment (Recital G), but refer to "the *mutual promises contained herein*" (Recital F) and place the RCMA at the very core of the overall transaction by stating that the Government's provision of financial assistance was contingent on receiving the promises in the RCMA, from petitioners as well as others (Recital E). Pet. App. 181a (emphasis added).

The Government's capital-credit assurance can only rationally be viewed as an enforceable promise under the RCMA—a "manifestation of intention" that "justif[ies] a promisee in understanding that a commitment has been made." *Restatement* § 2 & Comment b; *id.* §§ 3, 4, 202. As a common-sense matter, petitioners' RCMA commitments of their money, time, and reputations made no sense whatever without the Government's capital commitment. *United States v. Winstar*

Corp., 518 U.S. 839, 863 (1996) (plurality). Textually, moreover, under the RCMA's express characterization of the "*mutual promises contained herein*" (Recital F), the Government's capital-credit guarantee *had* to be an enforceable promise, because *there is no other Government promise in the document*. That fact alone disproves the Government's effort (unsupported by citation) to limit the RCMA § 1 "provided" commitment to the thrift and holding company (Opp. 13)—which is also wrong, legally and factually, on additional grounds as well. Thus, even if the Government's capital-credit commitment were viewed simply as benefiting the thrift and its holding company, black-letter law entitles petitioners to enforce it. *Restatement* § 305 Comment a ("[t]he promisee of a promise for the benefit of a beneficiary has the same right to performance as any other promisee"). And, in any event, the § 1 commitment runs to petitioners themselves, because RCMA §§ 4 and 7 put them on the line for the institutions' capital maintenance required by § 1, making clear that the Government's commitment was in exchange for petitioners' as well as the institutions' undertakings.[2]

2. On the merits, the Government strains to construct a justification for the Federal Circuit's damages ruling. Opp. 16-20. The various attempts ultimately rest on the same notion: that, because petitioners' *obligations* were limited under the RCMA, their damages must be limited to those obligations and cannot compensate them for their *opportunities* under the contract had it been performed. The Government offers this as another way of saying what the

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[2] The Government, while acknowledging that petitioners separately argued for breach of the RCMA capital-credit promise in the Federal Circuit, suggests that the brevity of the argument casts doubt on it. Opp. 16 n.4. To the contrary, the brevity reflects the simplicity of the point—which the Federal Circuit accepted, at least *arguendo*—as well as the need for space to address other more complex issues, including whether petitioners' contract went beyond the RCMA.

Federal Circuit said: that the breach-caused destruction of petitioners' property was not recoverable because the breached contract (the RCMA) did not require forfeiture (or initial acquisition) of that property. Like the Federal Circuit, however, the Government has cited not one authority for this limitation on contract damages—tacitly proving the novelty of the limitation on which the judgment below rests.

This limitation is not just unsupported but insupportable. By restricting protection of promisees' contract *opportunities* to their contract *obligations*, the Federal Circuit's and Government's new theory violates the core principle that distinguishes contract damages from tort and other damages. The essence of the well-established primary measure of contract damages, *i.e.*, expectation damages, is precisely to "give a plaintiff the full benefit of its bargain by compensating for forgone business opportunities." *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858, 873 (1986); *see Restatement* §§ 344, 347 & Comments a; R. Lord, *Williston on Contracts* § 64:2 (4th ed.) (promisee entitled to expected value of the contract if performed); E. Farnsworth, *Contracts* §§ 12.1, 12.9 (1982) (same, noting also UCC § 1-106(1)). The Federal Circuit's denial of damages, and the Government's defense of it, thus attack the very heart of contract-damages law, and the harmful consequences of the ruling are correspondingly large.

The RCMA bargain is plain. Petitioners made a continuing commitment—of their money (up to specified amounts), their time as directors and officers, and their reputations in the industry—to saving the thrift, a very risky proposition, benefiting the Government (which had no other bidders) by relieving it of an immediate liquidation liability. In exchange, petitioners received the Government's capital-credit commitment—without which it made no sense for petitioners to promise effectively to keep re-upping their investment each day after the April 30, 1987, RCMA—plus ownership of

what they might transform into a successful enterprise. The RCMA commitments, according to the RCMA itself, were central, not peripheral, to the whole transaction, for Recital E declares the Government's critical provision of financial assistance and indemnification to be conditional on those commitments. Pet. App. 181a. The basic rule of expectation damages guarantees petitioners the benefit of their bargain, and under standard contract law, those damages include the factually foreseeable destruction of their equity stake that was, in fact, caused by the Government's breach.

Two examples illustrate how far from settled law the Government has to reach. *First*: It suggests denial of relief because petitioners always faced a risk that they would have to forfeit their equity for the thrift to succeed. Opp. 18. This misses the critical point. Although contract parties always face risks that their enterprise will not succeed and they will suffer losses, contract law specifically protects against the causing of such business reversals and losses *by the actions of the other party breaching their promises in the contract.* Here, the Government's withdrawal of the capital-credit commitment, as the trial court found, is what caused petitioners' loss and thus renders the Government responsible. *Second*: The Government invokes the label "condition precedent" to describe its capital-credit commitment, Opp. 19, 21, as if that label defeated its liability for damages. This is sheer confusion. A "condition" in the Government's control, if not satisfied, might have relieved *petitioners* of *their* contract duties, but that is hardly the issue. The law of conditions has literally nothing to do with excusing non-performance by the party in control of the condition (let alone non-performance *after* the counterparty has performed, as petitioners had by committing their money, time, and reputations). *See Restatement* §§ 224-230.

The harmful consequences of the Federal Circuit's novel limitation on damages are evident. *See* Pet. 25-26. The rul-

ing will raise transaction costs in contracting, as parties must struggle to anticipate possible losses, write them into the contract, and perhaps even coordinate particular losses with particular obligations. It also will raise the contract price to the Government, as the increased transaction costs, plus the increased litigation costs and risk of limited recovery, must be compensated by higher payments in the contract. Not only private parties, but the Government itself will suffer. The Government does not dispute these evident harms—which will occur long before and outside the glare of further appellate rulings. Review is therefore needed now.

3. The ruling below also creates a deep intra-circuit conflict on a fundamental matter within the Federal Circuit's unique jurisdiction, an accepted basis for review. *See Cardinal Chem. Co. v. Morton Intern., Inc.*, 508 U.S. 83, 89 (1993).[3] Numerous Federal Circuit decisions articulate and apply, and award damages under, the ordinary expectation damages principle, without the novel restriction of damages to the plaintiff's contract obligations that was created and applied here. *See* Pet. 22-24. In the *Winstar* setting, both *Bluebonnet Sav. Bk. v. United States*, 266 F.3d 1348 (Fed. Cir. 2001), and *La Van v. United States*, 382 F.3d 1340 (Fed. Cir. 2004), do so. The Government tries to distinguish those decisions only by once again disputing that it made a promise to petitioners in the RCMA, a position the Federal Circuit here, for good reason, did not accept. Review is therefore

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[3] The United States has explained that, because of the Federal Circuit's special jurisdiction, "this Court has recognized the need for plenary review of Federal Circuit decisions that present issues of substantial importance. See, e.g., *United States v. Hill*, 113 S. Ct. 941, 945 (1993); *United States v. Goodyear Tire & Rubber Co.*, 493 U.S. 132, 138 (1989); *United States v. American Bar Endowment*, 477 U.S. 105, 109 (1986)." Petition for Certiorari at 14, in *United States v. IBM Corp.*, 517 U.S. 843 (1996), at 1995 WL 17013668.

needed not only because of harmful error on a fundamental issue, but also because of doctrinal conflict.

B. The Second Question Should Be Reviewed

1. The Government begins its response on the second question presented, as on the first, by trying to avoid the issue. It says (without citation) that petitioners did not contend in the Federal Circuit that the Board resolutions created contract rights, but argued only for incorporation of the resolutions in the Assistance Agreement. Opp. 22. That is wrong. Petitioners argued at length that they had (express and implied) contract rights from multiple sources, *i.e.*, the RCMA, the Board resolutions, and the Assistance Agreement (Doumani *et al.* Ct. App. Br. 15-19, 22-30 (May 25, 2004)), and specifically *denied* that they were relying on incorporation of the Board resolutions by the Assistance Agreement. *Id.* at 22 (Petitioners "do not sue for breach of the Assistance Agreement. Instead, they sue for breach of the Overall Contract, of which the Assistance Agreement was but one component."). Petitioners thus preserved the issue.

2. Even on the merits, the Government tries to divert attention from the actual issue. The question is not whether Government resolutions, regulations, or statutes *generally* give rise to contract rights. Opp. 24-25, discussing *National Railroad Passenger Corp. v. Atchison, Topeka & Santa Fe Ry.*, 470 U.S. 451 (1985). It is whether certain types of resolutions—which are common—do. The Government cites no authority whatever that denies such rights where, as here, the resolutions approve particular persons' financial transactions with and for the benefit of the Government, address the persons who made the offer to the Government, and impose duties on those persons as part of the transaction.

As the Government recognizes, the *Winstar* plurality treated the Board resolutions as sufficient to create contract rights. Opp. 25-26. And contract law makes clear that they

are. Contrary to the Government's citation-less statement, the absence of "agrees," "contracts," or "promises" language, let alone of language separately "requiring payment of damages," Opp. 23, in no way defeats contractual enforceability where "the realities of the transaction favor[ ] reading those documents as contractual commitments." *Winstar*, 518 U.S. at 863 (plurality). Contract enforceability depends not on the form of words but on a common-sense understanding that the actions are justifiably viewed as commitments. *Restatement* § 2 & Comment b; *id.* §§ 3, 4, 202; *see* Pet. 28. The Government does not identify a single one of the required elements for contract formation that is somehow missing in the Board resolutions.

When petitioners assumed the various duties imposed on them by the resolutions, they were justified in relying on the resolutions' assurances about capital regulatory treatment as enforceable commitments, without which petitioners' commitments would have been economically irrational. The presence of *additional* documents that serve various purposes *partially* overlapping with the resolutions is not uncommon and does not change the contractual nature of the resolutions. And recognizing the resolutions as contracts does not undermine the separate treatment of the institutions and the individuals, who have different duties and benefits under the various resolutions and separate agreements. *Contra* Opp. 24. The Assistance Agreement, providing for a monetary infusion into the institutions, creates one set of duties and rights; the RCMA, addressing other issues, creates others (for petitioners and the institutions); and the resolutions create still others (including duties for petitioners beyond those imposed by the RCMA). *See* Pet. 6.

3. Other Federal Circuit decisions, notably *Home Savings of America v. United States*, 399 F.3d 1341 (Fed. Cir. 2005), and *La Van*, *supra*, have held that Board resolutions create contract rights, without additional privately signed agree-

ments. *See* Pet. 28-29. The Government cannot distinguish those decisions, which it acknowledges held Board resolutions to create contract rights. Opp. 26-28.

As to *Home Savings*, the Government focuses on the particular private duties imposed by the resolutions ("full financial responsibility"). Opp. 27. But the particulars of the duty are immaterial: here, too, the resolutions imposed duties on petitioners, which differ only in detail, not in their role as defining a bargain that makes the Board resolutions enforceable. As to *La Van*, the Government notes aspects of the opinion (*e.g.*, about state law regarding veil piercing), Opp. 27-28, that have nothing to do with the legal issue here: whether Board resolutions just like the resolutions here create enforceable contract rights. *La Van*, like *Home Savings*, but contrary to the ruling in this case, squarely held that they do. The second question should thus be taken along with the first.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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